THE INFLUENCE OF OWNERSHIP STRUCTURE AND CORPORATE GOVERNANCE REFORMS ON PROFITABILITY AND MARKET VALUE OF PRIVATIZED COMPANIES IN KENYA

Gitundu Esther Wanjugu ✉

Department of Accounting, Finance and Management Science, Egerton University

Egerton, Kenya

ewgitundu@yahoo.com

Kibet Lawrence Kangogo

Department of Economics, Egerton University, Egerton, Kenya

Kiprop Symon Kibet

Department of Economics, Egerton University, Egerton, Kenya

Sifunjo E. Kisaka

Department of Finance and Accounting, University of Nairobi, Kenya

Abstract

This study examined the influence of ownership and corporate governance reforms on profitability and market value of privatized companies in Kenya. Data was obtained from financial reports of privatized companies and analyzed using Stata version 11. A unit root test was used to examine stationarity of data while a fixed effects regression model with a robust standard error option was applied to control errors which could bias results. The results indicate that government ownership and board composition have a positive effect on Returns on Assets (ROA) and on the Tobin's Q while women directors have a negative effect on ROA. This study recommends that the government should retain some ownership in privatized firms due to its unique role of enhancing security of shareholders investments. Diversity in corporate boards should be enhanced to attract managerial and technical expertise from non-executive directors to improve shareholder returns and the market value of privatized companies.

Keywords: Privatization; State Owned Enterprises; Ownership; Corporate Governance: Kenya

INTRODUCTION

The economic justification for privatization of State Owned Enterprises (SOEs) runs parallel to redefinition of the objectives of a company. According to Jensen and Meckling (1976) a firm exists to maximize shareholder's returns and its market value. In redefining corporate objectives, ownership and governance have become the core drivers of the value creation process. Privatization is supported by economic theories which point out weakness associated with state ownership. The property rights theory asserts that ownership and control in SOEs is widely separated which makes it difficult for the government to supervise managers and civil servants. The public choice theory infers that the politicians impose welfare and political objectives to SOEs for their own interests. The Agency theory infers that the separation of ownership and control gives managers opportunities to pursue their private interests more than that of the shareholders. The theories propose use of private ownership and corporate boards to improve the financial performance.

The question of how the ownership influences profitability and firm market value has attracted numerous studies using Return on Assets (ROA) and the Tobin's Q as performance indicators. The results are however conflicting. Some studies found that state ownership has a negative effect on profitability and firm value (Pervan *et al.,* 2012; Mishari *et al.,* 2012). However, others found that large state ownership influences performance positively (Trien & Chizema, 2011; Mei, 2013). Some studies conclude that institutional ownership influences financial performance positively (Alireza *et al.*, 2011; Uwuigbe & Olusanmi, 2012). However, other studies report negative influence (Wei *et al.,* 2005; Alipour & Amjadi, 2011). In addition, Omran *et al.* (2008) found that foreign investors had no significant influence on performance while Wei *et al.* (2005) found that they had a positive influence.

The effect of corporate governance on financial performance has also attracted empirical questions and previous studies have yielded inconsistent results. A number of studies document positive association between board size and firm performance (Adams & Mehran, 2011; Shukeri *et al.,* 2012). However others found insignificant relationships (Chaghadari; 2011; Latief *et al.,* 2014). Several studies report positive relationships between Non Executive Directors (NEDs) and financial performance (Agyei & Owusu, 2014; Lekaram, 2014). Apparently, other studies document negative associations (Fauzi & Locke, 2012; Rashid *et al.,* 2010; Shukeri *et al.,* 2012). Some studies found that women directors influence performance negatively (Mirza *et al.* 2012; Yasser, 2014). In contrast, Campbell and Mínguez (2008) document positive relationship. Lack of consensus on empirical evidence is not surprising as performance may depend on emerging ownership and corporate governance structure which may differ across firms.

Privatization in Kenya was adopted as a fiscal policy to reform ownership and corporate governance to enable privatized firms to make profits and increasing firm value (GoK, 1992; GoK, 2005). The interest of policy makers currently is to establish whether these reforms jointly or individually influence performance of privatized companies. However previous privatization studies in Kenya compare the pre and post performance of companies (Ochieng & Ahmed, 2014: Yaw & Toroitich, 2005). This study improves on previous research by examining the influence of emerging ownership and corporate governance structures on profitability and market value of privatized firms in a single regression model. The study also focuses on shareholder groups and corporate board variables which have potential to individually or jointly influence firm performance. The study also uses the most recent panel data and employs econometric approaches that address potential biases which could be caused by non stationary, heteroskedasticity and contemporaneous correlations in data values. The paper is divided into six sections. Section 1 presents the introduction, section 2 literature review and section 3 the methodology. Section 4 presents results and discussion, section 5 the conclusion and recommendations for policy while section six outlines potential areas for further research.

LITERATURE REVIEW

Privatization is supported by theories that depict private ownership as more efficient than public ownership. The property rights theory asserts that ownership rights in public enterprises are not specified which means that rewards and costs do not accrue to individuals (Alchian & Demsetz, 1973). Consequently, the public has no incentives and motivation to monitor managers and firm performance. The government as an owner is also considered inefficient due to the wide separation between ownership and control which makes it ineffective in monitoring managers (Shleifer & Vishny, 1997). Inefficiency in SOEs has also been attributed to reliance on government funding as the discipline enforced on private firms by the money and capital markets does not affect them (Sun & Tong, 2002). Privatization is therefore expected to improve the shareholders returns and firm value by transferring the management and control to private investors and corporate boards.

The public choice theory asserts that politicians and bureaucrats are motivated by private benefits and therefore use SOEs to advance interests such as maximization of votes and employment for their supporters (Tullock, 1967). Accordingly, extensive involvement of the state and politicians in the management of commercial enterprises impose welfare and political objectives on SOES which are contradictory to profit goals. According to Shleifer and Vishny (1997), political interference in public enterprises leads to overstaffing, poor choices of product and location, underinvestment and low incentives for managers to perform. Privatization is

expected to depoliticize privatized firms by passing ownership and control to private investors and corporate boards.

The agency theory points out that wide separation between ownership and management creates conflict of interests between the managers and shareholders. The theory developed by Jensen and Meckling (1976) asserts that the wide separation gives the managers opportunities to pursue private interests which may reduce profits and corporate value. The theory identifies large shareholders and corporate boards as mechanisms to protect shareholders interests, monitor managers and consequently increase returns and firm market value. Jensen & Meckling (1976) also indicate that corporate boards can effectively play their role if its size is small, has diverse skills, majority members are outside directors and the position of Chairman and CEO are separate. The role of corporate boards is also specified to include: monitoring managers, protecting shareholders interests and setting firm strategies firm (Fama & Jensen, 1983). The resource based theory identifies resources as a critical factor for a firm to enhance firm value. Barney (1991) defines the resources sought by firms to include technical expertise, managerial skills and information essential in detecting and responding to market opportunities. Privatization changes ownership and boards to help firms co-opt the skills and technologies from private investors and directors from outside the organization.

There are several empirical studies which examine the influence of private and public ownership structures on firm performance using ROA and Tobin's Q as performance indicators. Wei, *et al.* (2005) examined the relation between ownership structure and firm value of privatized firms in China and found that the state and institutional ownership had a negative influence on the Tobin's Q while foreign ownership had a positive effect. Ang and Ding (2006) compared market value of SOEs and private firms in Singapore and found that SOEs had a higher value compared to private firms. Tian and Estrin (2008) examined the influence of retained state shareholding on corporate value in China and found that firm value increased when state shareholding was large. Similarly, Trien and Chizema (2011) found that at low levels of state ownership, the Tobin's Q and ROA was negative, while it was positive when state ownership was high. In a different study, Alipour and Amjadi (2011) found a negative association between institutional and individual shareholders on performance of listed firms in Tehran.

In some more recent studies Mrad and Hallara (2012) examined the relationship between the government ownership and performance of privatized firms in France and found that high state ownership had a positive effect on ROA and the Tobin's Q. Mishari *et al.* (2012) explored the effects of ownership structure on ROA and Tobin's Q of listed firms in Kuwait and found that institutional investors influence performance positively while the government had a

negative impact. In Nigerian, Uwuigbe and Olusanmi (2012) found that institutional investors had a positive effect on ROA while foreign ownership had positive effect only on firms in the financial sector. In Croatian, Pervan, *et al.* (2012) found that firms with dispersed ownership had a higher ROA than those with concentrated ownership. Foreign controlled firms performed better than firms with high domestic ownership while firms with majority state ownership performed worse than privately held firms. In China Mei (2013) found that a higher state ownership had a better influence than dispersed ownership on ROA, Return on Equity (ROE) and the Tobin's Q. In Kenya, Ongore *et al.* (2011) found that state ownership had a negative effect on financial performance while foreign, insider, diverse and institutional ownership had a positive influence on ROA and ROE of firms listed firms. Mang'unyi (2011) found that foreign-owned banks had better performance than locally owned banks while Kiruri (2013) found that state ownership had negative effects on bank profitability while foreign ownership and domestic ownership had a positive influence.

Governance variables widely used on studies examining the relationship between corporate governance and firm performance include: size, board composition and gender diversity. In most of the studies, financial performance is measured using ROA and Tobin's Q ratio. Using this empirical approach, Campbell and Mínguez (2008) found that women directors had a positive effect on Tobin's Q in Spain while Carter *et al.* (2010) found no significant association between gender composition and ROA and Tobin's Q in US corporations. Rashid *et al.* (2010) found that NEDs added no value to the firm's performance in Bangladesh. Adams and Mehran (2011) found that the NEDs had no significant effect on the Tobin's Q while board size had a positive influence. In similar studies, Chaghadari (2011) found that NEDs and board size had no significant effects on performance measured by ROA and ROE in Malaysia. Fauzi and Locke (2012) found that board of directors and board committees had a positive impact on Tobin's Q and ROA while NEDs and female directors lowered performance of listed firms in New Zealand.

More recently, Shukeri *et al.* (2012) examined the impact of board composition on ROE of listed firms in Malaysia and found that board size has a positive relationship while NEDs had negative relationship with ROE. The study also found that gender diversity had no significant influence on firm performance. In Pakistan, Mirza *et al.* (2012) found that the percentage of women directors was negatively related to ROA and ROE of listed firms. Using the same approach, Agyei and Owusu (2014) found that board size and board composition, were positively related to performance in Ghana while Latief *et al.* (2014) found that NEDs and board size had no significant impact on ROA and ROE of privatized firms in Pakistan. Yasser (2014) found no significant relationship between gender diversity and firm performance in Pakistan

while Terjesen *et al.* (2015) found that firms with more women directors had a higher Tobin's Q and ROA in a sample of firms drawn from Taiwan, Turkey, Britain and United States. In Kenya, Miring'u and Muoria (2011) found a positive relationship between board size NEDs and ROE and of SOEs in Kenya while Letting *et al.* (2012) found no significant relationship between of board diversity and ROA of listed companies. Lekaram (2014) found that board size was negatively related to ROA and Tobin's Q while NEDs were positively related to Tobin's Q of manufacturing firms listed at the NSE. It is apparent that the studies examining the effects of ownership and corporate governance use separate regression models and also yield inconsistent results. Some studies document positive relationships, others negative effects while other authors find insignificant results.

METHODOLOGY

This study used a balanced panel data with observations for 8 privatized firms for the period 2007 to 2013. A defined criterion was used to select privatized firms from a population of all 55 listed companies in Kenya. The companies selected were those privatized by sale of shares, listed at the NSE, the GoK has retained some ownership and had published their annual reports. Ownership variables extracted from the annual reports were the percentage of shares owned by state, local institutions foreign institutions, large individuals and dispersed shareholders. Financial performance variables used in the regression models are ROA and the Tobin's Q. The values of ROA were computed by dividing profit after tax by total assets for each company for each year during the period 2007 to 2013. The values of profit after tax and total assets were extracted from the annual reports. The Tobin's Q ratio was computed by dividing market capitalization (total shares of a company at end of financial year multiplied by the share price) by the total assets. The share price data was extracted from NSE handbooks for 2008; 2012 to 2013 and 2013 to 2014. This study integrated other key variables in the regression model that have been found in literature to have significant effect on financial performance. These variables are the firm size, leverage and the investment levels of privatized companies. The Stata Version 11 was used to analyze data. A major concern while using panel data was non- stationary of data which may lead to spurious relationships. The Levin, Lin, Chu and (LLC) test was used to examine stationary in data values. The Fixed Effects (FE) was used to control for firm individual characteristics. The following regression equations were used.

$$\text{ROA}_{it\ it} = \alpha_0 + \alpha_1 \text{GOVT}_{it} + \alpha_2 \text{INST}_{it} + \alpha_3 \text{FORI}_{it} + \alpha_4 \text{LISH}_{it} + \alpha_5 \text{DISP}_{it} + \alpha_6 \text{BSIZE}_{it} + \alpha_7 \text{COMP}_{it} + \alpha_8 \text{GEND}_{it} + \alpha_9 \text{LNFSIZE}_{it} + \alpha_{10} \text{LEV}_{it} + \alpha_{11} \text{INVE}_{it} + \varepsilon_{it} \qquad (1)$$

Tobin's Q $_{it}$ $= \alpha_0 + \alpha_1 GOVT_{it} + \alpha_2 INST_{it} + \alpha_3 FORI_{it} + \alpha_4 LISH_{it} + \alpha_5 DISP_{it} + \alpha_6 BSIZE_{it} + \alpha_7 COMP_{it} + \alpha_8 GEND_{it} + \alpha_9 lnFSIZE_{it} + \alpha_{10} LEV_{it} + \alpha_{11} INVE_{it} + \varepsilon_{it}$ **(2)**

The variables and coefficients used in the regression models are measured as follows:

ROA   =   Profit after tax divided by total assets

Tobin's Q =   Market capitalization (shares at year end multiplied by share price / by total assets

α_0 =   Intercept or constant

α_1 =   Coefficients for each of the independent variables to be estimated: i =1-11

i   =   Individual company

t   =   Time (year)

GOVT =   Percentage of shareholding held by government in firm i in period t.

INST   =   Percentage shares owned by local institutions in firm i, in period t.

FORI   =   Percentage shares owned by foreign companies in firm i, in period t.

LISH   =   Percentage of shares held by large individual shareholders in firm i in period t.

DISP   =   Percentage of shares held by dispersed shareholders in firm i, in period t.

BSIZE   =   Total number of directors on the corporate board

COMP =   Percentage of non executive directors on the corporate board

GEND   =   Percentage of women directors in the corporate board

FSIZE   =   Total assets of a company (the log of total assets)

LEV   =   Total liabilities / total assets

INVE   =   Capital expenditure/ total assets

ε_{it} =   Error term

RESULTS AND DISCUSSION

The Descriptive Statistics

Table 1 below presents the mean, the standard deviation, minimum and maximum values of ownership structure, corporate governance, control and performance variables of privatized firms for the period 2007 to 2013.

Table 1: Descriptive Statistics

Var	Obs	Mean	Std. Dev.	Min	Max
Panel A: Ownership Structure of Privatized Companies					
Government	56	41.1	23.086	10.45	71.32
Institutional	56	10.47	13.347	0	49.63
Foreign	56	8.55	14.768	0	41.02
Large individuals	56	1.01	1.152	0	4.79
Dispersed	56	38.87	17.809	0	72.59

<div align="center">Panel B: Corporate Governance of Privatized Companies</div>

Board size	56	9.98	1.555	6	12
Board composition	56	.859	.070	.7	1
Gender composition	56	.180	.105	0	.4286

<div align="center">Panel C. Firm Size, Leverage and Investment of Privatized Companies</div>

Firm size	56	17.874	. 969	16.154	19.783
Leverage	56	.619	.215	.239	.890
Investment	56	.066	.085	.0004	.309

<div align="center">**Panel D: Financial Performance of privatized companies**</div>

ROA	56	.052	.054	-0641	.2129
Tobin's Q	56	.471	.492	0	2.132

The descriptive statistics show that the government is the largest share holder with an average of 41.1 % ownership followed by dispersed shareholders owning 38.87% of shares. The remaining 10.47 % is owned by local institutional investors, 8.55 % by foreign investors and 1.01 % by large individuals. These results are consistent to studies which found that the state remains the major shareholder in privatized firms (Tian & Estrin, 2008; Wei *et al.,* 2005). They are also consistent to studies which document large dispersed ownership in privatized companies (La Porta *et al.,* 1999; Faccio & Lang, 2002). The average board size of 9.98 is considered large compared to an average of 6.07 in New Zealand observed by Fauzi and Locke (2012) and 7 in Nepal reported by Ravi and Hovey (2013).

The average percentage of NEDs in privatized firms is 86% which is consistent to studies which document majority NEDs in corporate boards (Chaghadari, 2011; Fauzi & Locke 2012; Agyei& Owusu, 2014). Women directors comprise of 18% which is lower than the constitutional requirement of 30% in Kenya. The average ROA is 5.2% which is lower than the 7.17% documented by Sun and Tong (2002) in Malaysia.

The Tobin's Q of privatized firms in Kenya is 47.1 % which is lower than 82.9% observed by Mrad and Hallara (2012) in privatized French firms. This study integrated other variables in the regression model that have potential to influence financial performance. The average firm size expressed as the log of total assets of the companies is 17.87; leverage is 61.9% while the percentage of investment is 6.6%.

Panel Unit Root Test

This study used the LLC test to examine stationary. Table 2 below is a summary of the unit root test results.

Table 2: The Results of the Unit Root Test

Variable	1(0) Adjusted t	P- value	1(1) Adjusted t	P-value
Panel A : The Unit Root Tests for the Ownership Variables and Financial Performance of Privatized Companies				
ROA	-2.9722	0.0015		
Tobin's Q	-6.3857	0.0000		
Government	175.9886	1.0000	507.2046	1.0000
Institutional	-3.6325	0.0001		
Foreign	-1.9067	0.0283		
Large individual	-0.0949	0.4622	-2.9244	0.0017
Dispersed	-51.2902	0.0000		
Board size	-3.5133	0.0002		
Board Composition	-4.9976	0.0000		
Gender	-0.0445	0.5178	-2.3497	0.0094
Firm size	1.0494	0.8530	-5.3204	0.0000
Leverage	-2.4433	0.0073		
Investment	-3.8166	0.0001		

The results for ROA, Tobin's Q institutional, foreign, and dispersed, board size, board composition, leverage and investment were stationary in their first level form as the p-values are less than the critical value of 0.05. The p-values for government, large individual, gender and firm size, were more than the critical value of 0.05 implying that they had unit roots. The variables were then subjected to a first level difference under which firm size and large individual achieved stationarity. The differenced values were then used in the regression models. The government remained non stationary and could not be differenced further as the unit root test requires a minimum of six (6) panels. The variable was therefore used in the regression models in its original form. The unit root tests show no co-relationship among differenced values and hence the co-integration test was not necessary.

The Influence of Ownership Structure and Corporate Governance on ROA of Privatized Companies

Table 3 presents the results of regression models for the relationship between ownership structure, corporate governance and financial performance of privatized companies. Panel A presents the regression results of the influence of ownership structure and corporate governance on the ROA while Panel B shows the effects on the Tobin's Q. The results include the coefficients of individual variables, robust standard error estimates; the coefficient of determination, R^2; F-statistics and the *t*-statistic.

Table 3: The Effects of Ownership and Corporate Governance on Profitability and Market Value of Privatized Companies.

Panel A: The effects of Ownership and Corporate Governance on ROA.				
ROA	Coef.	Robust Std. Err.	t	Prob.Value
Government(lag1)	.0017*	.0009	1.98	0.088
Institutional (lag1)	.0035	.0021	1.62	0.149
Large individual	.0006	.0044	0.13	0.903
Board size (lag1)	.0101	.0083	1.22	0.262
Board composition	.1438**	.0507	2.83	0.025
Gender(lag1)	.0506	.0334	1.51	0.175
Firm size	-.0406	.0621	-0.65	0.534
constant	-.2841*	-1411	-2.01	0.084
R^2= 0.1211		F=202.13		Prob> F = 0.0000
Panel B: influence of Ownership and Corporate Governance on the Tobin's Q				
TOBIN'S Q	Coef.	Robust Std. Err.	t	Prob.Value
Government	.0142**	.0053	2.69	0.031
Institutional (lag1)	.0167	-0162	1.03	0.338
Large Individual	.0322	.0547	0.59	0.574
Board size(lag1)	.1018	.0885	1.15	0.288
Board composition (lag1)	1.5386**	.6196	2.48	0.042
Gender (lag1)	.6706	.4757	1.41	0.201
Firm size	-.2588	.1869	-1.38	0.209
constant	-2.695	1.6611	-1.62	0.149
R^2=0. 2686		F=151.88		Prob> F = 0.0000

The Effects of Ownership Structure and Corporate Governance on ROA of Privatized Companies

Panel A presents the results of the combined and individual effects of ownership and corporate governance structures on ROA. An FE regression model with a robust standard error option was used to controls for individual firm characteristics which could be sources of heteroscedasticity and contemporaneous correlation which could influence ROA. The FE model eliminated foreign ownership as most of the values were not varying with time. Dispersed ownership, leverage and investment were also automatically eliminated from the model probably because they were not significant. The model was significant when the lagged values of government, institutional ownership, large individual investors, and board size and gender composition were used. This implies that the past values of the variables (government, institutional, large individual investors, and board size and gender composition) influence ROA. The F value is significant at 1% level which implies that the joint effect of ownership and

corporate governance variables ROA was significant. The fitted model explained only 12.11% of the variance in ROA.

The *t*-tests for individual coefficients show that government ownership has positive influence on ROA at 10% level. This is contrary to the propositions of the property rights and the public choice theories which depict government ownership as detrimental to financial performance. However, from an agency theory perspective, large ownership gives the government stronger power to monitor managers in a system with a large number of dispersed shareholders. The dispersed shareholders own 38.87% which could potentially generate agency problems in a firm as they do not have capacity to collectively monitor managers. The method used by shareholders to monitor and influence corporate governance is through board representation. With a 41.1% ownership, the government holds nearly half of the seats in corporate boards. This means that the government can easily influence passing of ordinary resolutions as they require a simple majority of 51%. The government can also nominate nearly a half of the board of directors implying that can influence decision making of boards which involve setting strategies and policies, appointing senior managers, monitoring performance and approving budgets.

A positive influence may also indicate that the government can also collaborate with private investors to influence performance positively. The GoK shares are held by the Treasury which is expected to exercise its powers as a shareholder in monitoring managers and influencing decision making in corporate boards. It is also likely that the government as an owner decreases the likelihood of expropriation of corporate assets by managers. The results are consistent with previous studies which found that large government ownership has a positive influence on ROA (Trien & Chizema, 2011; Tian & Estrin, 2008).

The institutional ownership has an insignificant effect on ROA. These findings contrast the property rights theory which considers institutional investors to be more effective in monitoring managers and focused on generating profits. A number of studies also found that institutional shareholders influence profitability of firms positively (Kiruri 2013; Mishari *et al.,* 2012; Ongore *et al.* 2011). The insignificant relationship could however be ascribed to the small size of ownership held by institutional investors. Although institutional are expected to enhance managerial monitoring, their effectiveness may be hindered by inadequate representation in corporate board. The institutional investors own 10% which implies that they are only entitled at least one director to the board which may not have significant influence on boards. This means that they are not able to influence decisions making that involve: setting strategies, appointment of top managers and approval of budgets. The large individual shareholders have an insignificant influence on ROA which confirms the agency theory view which asserts that

individual shareholders have no capacity to monitor managers or influence firm decision making process. Large individuals hold a mean of 1% ownership in privatized firms an indicator that they have small ownership and control rights in a firm. This means that they have no capacity or monitor the managers or influence decision making in corporate boards.

The board size has an insignificant influence on ROA. This contrasts the agency theory which views large boards as harmful to performance due to difficulties in coordination, flexibility and communication. The insignificant findings may imply that the negative effects of a large board may be cancelled out if members of the board bring additional skills which could improve the decision making and monitoring of managers. The results are similar to other studies which found no significant association between board size and ROA (Chaghadari, 2011; Latief *et al.* 2014). The NEDs have a positive effect on ROA at 5% significance level. This means that NEDs is an important determinant of firm performance. From a resource based theoretical perspective, the NEDs may have helped the privatized firms to attract skills and resources crucial to firm performance. These results are similar to studies which document positively relationships between NEDs and financial returns (Agyei & Owusu 2014; Miring'u & Muoria, 2011).

The women directors have an insignificant relationship with ROA. These findings suggest that gender alone may not a major determinant ROA. From the agency theory and the resource based theoretical perspectives, privatized firms had not achieved a composition of women directors to influence corporate boards in decision making. The findings are similar to other studies which document insignificant association between women directors and financial performance (Carter, *et al.,* 2010; Yasser, 2014). Firm size as a control variable has an insignificant effect on ROA which could imply that the benefit the large size is cancelled out by bigger bureaucracy and managerial problems associated with large firms which increase costs.

The Influence of Ownership Structure and Corporate Governance on the Tobin's Q of Privatized Companies

Panel B presents the results of the regression model examining the effects of ownership and corporate governance on the Tobin's Q. An FE regression model with a robust standard error option was used to controls firm characteristic which be sources of heteroscedasticity, and cross sectional dependence of errors in data values. The FE model eliminated foreign ownership as most of the values were not varying with time. The dispersed ownership, leverage and investment were also automatically eliminated from the model probably because they were not significant. The model was stable when government, institutional ownership, large individual investors, board size and gender were lagged once. This is an indicator that the variables (government, institutional ownership, large individual, board size and women directors) one year

before could influence the current market value of privatized firms. The F value is significant at 1% level implying that the joint effect of the ownership and corporate governance on the Tobin's Q is significant. The fitted model however explained 26.86% of the variance in the Tobin's Q.

The results show that government has a significant relationship with Tobin's Q at 5% level. A positive relationship suggests that the government as a large shareholder enhances investors' confidence in a firm and may be preferred in a system where of a large number of shareholders is dispersed. The results may also suggest that by having a larger representation in corporate boards, the investors may be convinced that the government can use a wide range of measures to ensure investor protection and economic stability which may increase the market value of the share price. The investors may also value privatized firms positively as they belief that resources are likely to be used more efficiently if the state is involved in firm governance and therefore reduce chances of corporate failure. These finding are consistent to several empirical studies which also found that government ownership influences firm value positively (Ang & Ding, 2006; Wei, *et al.,* 2005; Tian & Estrin, 2008).

Institutional investors have an insignificant influence on Tobin's Q. The results contradict the resource based theory which considers institutional investors to be endowed with managerial and technical expertise with potential to enhance firm value. The insignificant results could however be attributed to the small size of ownership and lack of anchor institutional investors who could bring both technical expertise and managerial skills to influence performance. Institutional investors hold 10 % ownership in privatized firms and this may be held by several institutions. Consequently, their effectiveness may be limited by low representation in corporate boards. From the property rights theoretical view privatized firms have not passed sufficient control rights to private investors who are more focused in increasing the firm value.

Large individual investors also have an insignificant influence on the Tobin's. The results appear to concur with the agency theory which views individual shareholders to lack capacity to enhance firm value. The insignificant effects could be attributed to the small size of individual investors. This size is also insufficient to allow the large individual investors to be represented in corporate boards. The dispersed shareholders also have an insignificant influence on Tobin's Q. The results concur with the agency theory as it perceives dispersed shareholders to lack capacity to enhance firm value.

The board size has insignificant influence on the Tobin's Q and results are consistent with other studies which document insignificant associations between board size and firm performance (Chaghadari, 2011; Latief *et al.,* 2014). The findings suggest that investors' opinion may not be influenced largely by the size of corporate boards but rather by the independence of

the board as found in this study. The board composition has a positive influence on the Tobin's Q at 5% level. A positive effect is an indicator that the investors were reacting positively to the appointment of NEDs as a signal of independence and better firm management. This is also consistent with agency theory which suggests that boards with a higher size of NEDs may enhance firm value by monitoring the opportunistic behavior of managers. From the resource based theoretical perspective, NEDs are associated with securing resources and professional expertise crucial to increase corporate value. These results are similar findings other studies which found a positive relationship between NEDs and firm performance (Agyei & Owusu, 2014; Lekaram, 2014).

The women directors have an insignificant influence on the Tobin's Q which could be attributed to their small percentage as it may be insufficient to bringing technical skills and ethical considerations or influence decision making in corporate boards. This confirms the argument that gender alone may not have any significant influence on firm performance. The only control variable included in the regression model is firm size and has an insignificant effect on Tobin's Q. This could imply that the benefits of the large size were cancelled out by the inherent management of large companies as they are associated with bigger bureaucracy and managerial discretion which increases monitoring costs.

SUMMARY

This study examined the influence of ownership and corporate governance on profitability and market value of privatized firms in Kenya. The results confirm that ownership structure and corporate governance jointly influence firm performance. Among the individual variables, government ownership and board composition have a positive influence on ROA and the Tobin's Q. while women directors have a negative effect on ROA. This study recommends that the government should retain some ownership in privatized firms due to their unique role of enhancing shareholders confidence and protection of investments in a system with a high level of dispersed ownership. Although the constitution requires that 30% composition of women in corporate boards, the appointment should be based on qualification and professional expertise to ensure they contribute positively to firm performance. Diversity in corporate boards should be enhanced to attract managerial and technical expertise from NEDs which is crucial to improving profitability and the market value of privatized companies.

AREAS FOR FURTHER RESEARCH

There are a number of knowledge gaps arising from this study that need to be addressed through further research. One of the main issues is that the fitted models explained only a small

percentage of the variance in the dependant variables. Researchers could therefore extend the study by including in the regression models variables other governance variables such as managerial skills, education levels, skills diversity, ethnicity and age of top level managers. Similarly, ownership may be further explored by differentiating shares held by managers, directors, employees, and block-investors. Due to inconsistencies in results from previous studies, there is need for more current studies to establish the long term effects of privatization reforms on firm financial performance. Contrary to the prevailing theoretical opinion, this study found that government ownership enhances performance in business enterprises. There is therefore need for studies to explore potential benefits of collaboration between government and private sector in commercial activities.

REFERENCES

Adams, B. and Mehran, H. (2011). Corporate Performance, Board Structure and their Determinants in the Banking Industry. Retrieved on June 2 2013, from http://www.nyfedeconomists.org.

Agyei, A. & Owusu, R. (2014). The Effect of Ownership Structure and Corporate Governance on Capital Structure of Ghanaian Listed Manufacturing Companies. International Journal of Academic Research in Accounting, Finance and Management Sciences, (4), 109–118.

Alchian, A. & Demsetz, H. (1973). The Property Right Paradigm. The Journal of Economic History, 33, 16-27.

Alireza, F. Hendi, A, T. & Mahboubi, K. (2011). The Examination of the Effect of Ownership Structure on Firm Performance in Listed Firms of Tehran Stock Exchange. Journal of Business and Management, 6 (3), 249 -266.

Alipour, M. & Amjadi, H. (2011). The Effect of Ownership Structure on Corporate Performance of Listed Companies in Tehran Stock Exchange: An Empirical Evidence of Iran. International Journal of Business and Social Science, 2(13), 49-55.

Ang, J.S, & Ding, D.K. (2006). Government Ownership and the Performance of Government Linked Companies: The Case of Singapore. Retrieved February 20, 2014 from http://www.sciencedirect.com

Barney, J.B. (1991). Firm Resources and Sustained Competitive Advantage. Journal of Management, 17, 99-120.

Campbell, K. & Mínguez, V.A. (2008). Gender Diversity in the Boardroom and Firm Financial Performance. Journal of Business Ethics, 83, 435–451.

Carter, D A., D'Souza, F.K., Simkins B. J & Simpson, G. (2010). The Gender and Ethnic Diversity of US Boards and Board Committees and Firm Financial Performance. Corporate Governance: An International Review, 18(5), 396–414.

Chaghadari, M.F. (2011). Corporate Governance and Firm Performance. International Conference on Sociality and Economics Development, 10, 484-489.

Faccio, M. & Lang H.P (2002). The Ultimate Ownership of Western European Corporations. Journal of Finance and Economics, 65: 365–395

Fama, F. & Jensen, M. C. (1983). Separation of Ownership and Control. Journal of Law and Economics, 26: 301- 25.

Fauzi, F. & Locke, S. (2012). Firm Performance: A Study of New Zealand Listed Firms. Journal of Accounting and Finance, 8(2), 43–67.

GoK (1992). Policy Paper on Public Enterprises Reforms and Privatization. Retrieved April 2, 2013, Retrieved 12th June 2013 from http://www.pc.go.ke .

GoK, (2005). The Sessional Paper on Privatization. Retrieved April 21, 2013 from http://siteresources.worldbank.org.

Kiruri, R. M. (2013). The Effects of Ownership Structure on Bank Profitability in Kenya; European Journal of Management Sciences and Economics, 1(2), 116-127.

Jensen, M. & Meckling, W. (1976). Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure. Journal of Financial Economics, (3), 305-360.

La Porta, R. & López-de-Silanes, F (1999).The Benefits of Privatization: Evidence from Mexico. Quarterly Journal of Economics, 114(4), 1193-1242.

Latief, R., Syed, H., & Syed, A. (2014). Impact of Corporate Governance on Performance of Privatized Firms; Evidence from Non-Financial Sector of Pakistan .Middle-East Journal of Scientific Research 19 (3), 360-366

Lekaram, V (2014). The Relationship of Corporate Governance and Financial Performance of Manufacturing Firms Listed in the Nairobi Securities Exchange. Journal of Business and Commerce, (3)12, 30-57

Letting, N., Aosa, E. & Machuki, V. (2012). Board Diversity and Performance of Companies Listed in Nairobi Stock Exchange. International Journal of Humanities and Social Science, 2, 172-182

Mei, Y. (2013). State ownership and firm performance: Empirical evidence from Chinese listed Companies. China Journal of Accounting Research, 6: 75-87

Miring'u, A.N & Muoria, E. T. (2011). An Analysis of the Effect of Corporate Governance on Performance of Commercial State Corporations in Kenya. International Journal of Business and Public Management, 1(1), 36-41.

Mirza, H., Mahmood, S., Andleeb, S. & Ramzan, F. (2012). Gender Diversity and Firm Performance: Evidence from Pakistan. Journal of Social and Development Sciences, 3 (5), 161-166.

Mishari, A., Faisal, A. & Hesham, A. (2012). The Influence of Institutional and Government Ownership on Firm Performance: Evidence from Kuwait. International Business Research, 5 (10), 192- 200.

Mrad, M. & Hallara, S. (2012). The Impact of Residual Government Ownership on Performance and Value Creation: The Case of Privatized French Companies. Procedia - Social and Behavioral Sciences, 62, 473 – 488

Ochieng, M & Ahmed, A. (2014). Privatization in Kenya – The Effects of Privatization on the Financial Performance of Kenya Airways. International Journal of Business and Commerce, (3)5, 10-26.

Omran, M.M., Bolbol, A., & Fatheldin, A. (2008). Corporate Governance and Firm Performance in Arab Equity Markets: Does Ownership Concentration Matter? International Review of Law and Economics, 28, 32-45.

Ongore, V.O.,K'Obonyo, P. O.& Ogutu, M. (2011). Implications of Firm Ownership Identity and Managerial Discretion on Financial Performance: Empirical Evidence from Nairobi Stock Exchange. International Journal of Humanities and Social Science, 1,187-195.

Pervan, M., Pervan, I. & Todoric, M . (2012). Firm Ownership and Performance: Evidence for

Croatian Listed Firms. World Academy of Science, Engineering & Technology, 6, 1-28

Rashid, A., De Zoysa, L. Odh, S. & Rudkin, K. (2010). Board Composition and Firm Performance: Evidence from Bangladesh. Australasian Accounting Business and Finance Journal, 4, 76-95.

Ravi, P. S & Hovey, M. (2013).Corporate Governance and Efficiency in Nepalese Commercial Banks: International Review of Business Research Papers. 9(4), 53 – 64

Shleifer, A. & Vishny, R.W. (1997). A Survey of Corporate Governance. Journal of Finance, 52(2), 737-783.

Shukeri S., Shin, W. & Shaari, M, S. (2012). Does Board of Director's Characteristics Affect Firm Performance? Evidence from Malaysian Public Listed Companies. International Business Research, (5), 120-127.

Sun, Q. & Tong, W. (2002). Malaysia Privatization: A Comprehensive Study. Journal of Financial Management, 31, 79-105.

Terjesen, S., Barbosa,E. Couto P., & Morais, F. (2015). Does the Presence of Independent and Female Directors Impact Firm Performance? A Multi-Country Study of Board Diversity, Journal of Management and Governance, 10, 1-37

Tian, L & Estrin, S. (2008). Retained State Shareholding in Chinese PLCs: Does Government Ownership Reduce Corporate Value? Journal of Comparative Economics, 36, 74–89.

Trien, L. & Chizema, A. (2011). State Ownership and Firm Performance: Evidence from the Chinese Listed Firms. Organizations and Markets in Emerging Economies, 2, 72-90.

Tullock, G. (1967). The Welfare Costs of Tariffs, Monopolies, and Theft. Western Economic Journal, 5 (3), 224–232.

Uwuigbe, U. & Olusanmi, O. (2012). An Empirical Examination of the Relationship between Ownership Structure and the Performance of Firms in Nigeria. International Business Research, 5 (1), 208- 215.

Vickers, J. & Yarrow, G. (1991). Economic Perspective on Privatization. Journal of Economic Perspectives, 5, 111–132.

Wei, Z., Xie, F. & Zhang, S. (2005). Ownership Structure and Firm Value in China's Privatized Firms: 1991-2001. Journal of Financial & Quantitative Analysis, 40, 87-108.

Yasser, Q. (2014). Effects of Female Directors on Firms Performance in Pakistan. Modern Economy, (3), 817-825.

Yaw, A. & Toroitich, O.K (2005). The Making of an African Success Story: The Privatization of Kenya Airways. Thunderbird International Business Review, 47:205–230.