# INFLUENCE OF CORPORATE GOVERNANCE ON PERFROMANCE OF WATER COMPANIES IN KENYA: CASE OF MACHAKOS WATER AND SEWERAGE COMPANY

SUBMITTED BY

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A DISSERTATION SUBMITTED TO THE FACULTY OF BUSINESS AND COMUNICATION STUDIES IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF DEGREE OF MASTER OF BUSINESS ADMINISTRATION IN STRATEGIC MANAGEMENT AND LEADERSHIP OF ST. PAUL'S UNIVERSITY

MAY, 2018

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## DECLARATION

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## DEDICATION

I dedicate this work to my beloved husband Moses, our children Claire and Blair who have been a source of inspiration, supporting and understanding throughout my studies. I also dedicate to my parents and siblings for their support and encouragement all through.

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# LIST OF ABBRIVIATIONS AND ACRONYMS

| | |
|---|---|
| BSC | Balanced Scorecard |
| CEO | Chief Executive Officer |
| CMA | Capital Market Authority |
| IDRC | International Development Research Centre |
| MACHWASO | Machakos Water and Sewerage Company |
| NACOSTI | National Commission for Science, Technology and Innovation |
| NWSS | National Water Services Strategy |
| PSCGT | Private Sector Corporate Governance Trust |
| RBT | Resource Dependency Theory |
| ROA | Return on Assets |
| ROI | Return on Investment |
| SPA | Service Provision Agreement |
| SCs | State Corporations |
| SPSS | Statistical Package for Social Sciences |
| TAWSB | Tanathi2 Water Service Board |
| WASREB | Water Services Regulatory Board |
| WSP | Water Service Providers |

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# OPERATIONAL DEFINITION OF TERMS

| | |
|---|---|
| **CEO Duality** | CEO Duality is a structure in which the roles of the CEO and the chairman of the board are held by one individual. This helps to reduce conflict of interest, concentrates power to one individual hence reducing on agency costs. |
| **Corporate Governance** | Corporate governance is a system by which companies are directed and controlled. It sets out the relationship between the company directors, shareholders and other stakeholders by defining the controlling powers of the shareholders. |
| **Corporate Leadership** | Corporate leadership is the actions of the board that serve to move the organization forward towards maximization of the shareholders wealth. It signifies the manner in which the board provides direction, implements plans, formulates policies and motivates staff towards achievement of goals. |
| **Performance** | Performance is the execution and accomplishment of work, tasks or goals to a certain level of desired satisfaction. It is the realization of the set goals and objectives which helps in understanding the effectiveness of an organization. |
| **Non-Revenue Water** | Non-revenue water is water that is produced and lost through technical and commercial losses hence not billed. |
| **Water Service Provider** | Water service provider is a company, non-governmental organization or a person who provides water services and is licensed with water service board. |

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# ABSTRACT

There has been increased awareness on the concept of Corporate Governance and its effect on performance of public and private companies. This has been enhanced by the disclosure of major scandals affecting the corporate level of organizations leading to collapse or near collapse of large corporations. Corporate Governance helps to strike a balance between the interest of the management and those of other stakeholders. Water sector however has been on the fore front for consideration due to the nature of the industry's core business. This is because water is a basic commodity and its scarcity threatens the very nature of human kind. The performance of this sector is therefore of great importance to the Nation. Against this basis, this study sought to establish the influence of corporate governance on performance of water service providers. The specific objectives of this study sought to determine the influence of board structure, strategic roles of the board, corporate leadership and board independence on performance of Machakos Water and Sewer-age Company Limited. The study used descriptive research design employed on sixty respondents who were drawn from a target population of eighty five employees of the company. The respondents were selected from all cadres within the company. Stratified random sampling technique was used. The study used both primary and secondary data. Questionnaires were used for primary data collection. The secondary data was obtained from water sector published and unpublished reports. Drop and pick method was used to disseminate the questionnaires. Data was descriptively analysed and presented using percentages, measures of central tendencies, frequency distribution tables, figures and multiple regression analysis model. SPSS was used for analysis. The study established that there is gender parity in the company, the respondents were aware of the existence of the board and they viewed it to be of great importance. It sought to identify the relationship between the board structure, strategic roles of the board, corporate leadership and board independence of the overall performance of the company. It was found out that there was a statistical significance between the predictors and performance. Further, it was realized that strategic roles of the board had the greatest effect on performance accounting to 0.633 of the overall performance. On the indicators of performance used, the study established that the company had improved greatly on revenue growth with the highest rating of 4.12 compared to others. Out of the inferences drawn the researcher concluded that companies need to exploit the strategic roles of the board since it has the greatest and instant effect on performance.


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# CHAPTER ONE
# INTRODUCTION

## 1.1 Background of the Study

The performance of organizations reflects the economic well-being of a nation (Kiratu & Moronge, 2016). According to Al-Matari, Al-Swidi and Fadzil (2014), the success of a firm is explained by its performance over time which is significantly affected by corporate governance practices employed. Therefore, operations of a firm should be well established for the corporate governance system. Corporate governance is a phrase denoting the mechanisms through which companies are directed and controlled (Cadbury Report, 1992). Naimah and Hamidah (2017) asserts that corporate governance is system that is designed to direct the company professionally and is based on good corporate principles. These principles include transparency, accountability, responsibility, independence and fairness. Many scholars have defined corporate governance based on the characteristics of the organization being studied.

The focus on corporate governance originated in nineteenth century when organization was being prescribed as a limiting liability. Eckert (2005) asserts that corporate governance concerns commences immediately a company is registered. Much attention was directed to corporate governance in 1990s due to financial crisis that existed in East Asia and South America, and various corporate scandals that emerged in developed countries such as Italy and France (Samia & Salem, 2016). It increasingly became a critical issue for both developed and developing economies as it is critical in sustainability of firms, economic growth and development. Furthermore, globalization has led to increased focus on corporate governance since many nations desire to grow through gaining of resources from both domestic and international levels.

Corporate governance practices are essential elements that act to strengthen the foundation of strategic economic performance of countries and organizations (Pletzer, Nikolova, Kedzior & Voelpel, 2015). The contribution of corporate governance to the growth and development of economy in nations has become a contemporary issue. Cleasssens and Yurtoglu (2013) asserts that lack of poor corporate governance is the leading cause of failure in organizations. Furthermore, existing literature supports the

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role of good corporate governance in impacting on organizational performance. Therefore, corporate governance practices cannot be over emphasized as one of the key elements that has derailed economic growth and development of countries Kenya included.

In Kenya, just as in other developing countries, corporate governance, has gained primacy (Ekadah & Mboya, 2011).The various corporate scandals have been ascribed to poor corporate governance, lack of proper controls in organizations and conflict of interest. The Private Sector Corporate Governance Trust (PSCGT) has been the greatest advocate in corporate governance in Kenya (PSCGT, 1999).The concept of governance in Kenya started in 1999 with the development of Centre for Corporate Governance- Kenya, which led to development of a framework for adoption by companies. Further, the Capital Markets Authority (CMA) in 2000 formulated practices of corporate governance which were concerned with handling issues related to the directors. These issues included the composition of the board, separation of the responsibilities of CEO and chairman, as well as establishment and definition of the roles of audit committee

The water sector in Kenya underwent major reforms in a bid to ensure efficient and sustainable delivery of services. As a result, the reforms led to enactment of Water Act 2002 which resulted to institutional framework on water service provision (Water Act, 2000). Thus, water resources were commercialized to enhance decentralization of processes as well as stakeholder participation in managing the national water resources (Moraa, Otieno & Salim, 2012). This further led to creation of Water Services Regulatory Board (WASREB) which provides rules and enforces standards in the provision of water services so that there is protection of consumers, affordable and sustainable access to efficient services (WASREB, 2003). Water service providers (WSPS) have hence adopted the corporate governance guidelines as stipulated by the regulator. Some companies have been successful in implementing these corporate governance while others have been met with resistance. Thus, WSPs have not met the requirements of Vision 2030 in terms of their efficiency and effectiveness in service delivery. This phenomenon could be attributed to weak corporate governance practices in the sector.

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### 1.1.1 Corporate Governance

According to Gachoki and Rotich (2013), corporate governance is defined as combination of corporate policies and best practices that a corporate entity adopts with the aim of realising the set objectives and meeting the expectations of their stakeholders. It is a critical concern for all corporations as it since it is a key element to corporate success. The Cadbury Committee (2002) of United Kingdom asserts that corporate governance is a system through which companies are directed and controlled. The day to day running of businesses in the corporate world is based on fulfilling the expectations of various stakeholders and involves compliance with legal requirements and demonstrating ethical conduct (Aggarwal, 2013). Therefore, corporate governance can be defined as a set of relationships that exist between the directors, management and stakeholders in an organization.

According to PSCGT (1999), corporate governance is explained as the way in which the corporate power is administered in the stewardship of the total assets and resources of an organization. It is mainly concerned with maintaining and increasing value and satisfaction of the shareholders as per the corporate's mission statement. Corporate governance is concerned with ensuring that a balance between economic and social goals has been maintained and that there is proper utilization of resources as well as accountability (Pletzer *et al.*, 2015).

Governance is concerned with encouraging corporate sector to be accountable, transparent, fair and responsible (Trickler, 2015). Furthermore, according to Pletzer et al., (2015) most companies have established the concept of corporate governance which comprises of major components including rules and regulations, Chairman and CEO roles, board of directors, fairness, accountability and transparency of the operations of the business. With effective corporate governance, transparency, credibility and accountability are reinforced hence the success of an organization (Samia & Salem, 2016).

Gachoki and Rotich (2013) points that organizations should design corporate governance frameworks that are secure and benefits all shareholders and those that monitor the management performance so as to maximize on wealth. The board of directors serves as a link that connects the owners of the business and managers.

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Corporate governance should promote good governance standards that focus on attracting financial resources, reducing risk and developing organizational performance (Ahmed & Hamdan, 2015). As such proper, practices should be adopted in organizations so as to enhance performance as they impact on performance (Naimah & Hamidah, 2017). The practices of corporate governance include the board of directors who monitor and supervise the management. The board composition should have optimal number of directors majority of which are independent and an audit committee which monitors and controls the operations and enhances accountability. The responsibilities of the CEO and chairman should be held by different individuals so as to enhance good corporate leadership and for effective decision making as well as implementation and controls (Muriuki, Cheruiyot & Komen, 2017).

In the water sector, effective corporate governance is demonstrated by presence of board of directors who have expertise and experience that are necessary to accomplish the effective performance (WASREB, 2003). The board structure which comprises of optimal number of directors, frequency of meetings and diversity in skills mix and experience. Board independence is ascertained through inclusion of independent directors and audit committee. The board is led by the chairman whose roles are separated from the CEO thus decisions are made independently.

### 1.1.2 Performance

Performance is the realization of tasks or set goals to certain levels of anticipated satisfaction (Kiratu & Moronge, 2016). Organizations are formed with the aim of achieving specific goals and objectives. They represent a voluntary interaction of production assets comprising of human resources and capital resources primarily for achieving the set goals and shared purpose. Venkatraman and Ramanujam (1986) assert that companies engage in business and various ventures to succeed. Thus the performance of an organization is a crucial aspect and is at the heart of the strategic management.

The performance of an organization is an indicator of its effectiveness (Machuki and Aosa 2011). Organizational performance can be determined by measuring some of its

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indicators including; realization of financial goals, efficiency in service delivery and social responsibilities extended to the stakeholders. According to Trickler (2015), measuring of organizational performance is faced by challenges due to organizational diverse roles and responsibilities giving a multidimensional contrast hence difficulty to measure.

The principal objective of organizational performance is to increase effectiveness and efficiency in service delivery of an organization. Performance measurement is key in an organization as it plays a key role in achievement of the goals and objectives. In most cases, performance is usually measured by qualitative and quantitative evaluation of values of performance indicators (Maharm & Anderson, 2008). Therefore, a company should establish the relevant indicators of performance, show the relationship between these indicators and its goals as well as determine how they can be measured.

Organizational performance is an indicator of a company's efficiency and effectiveness, financial health and relevance. The effectiveness of a firm is a result of the unique capabilities and or strengths which a firm acquires to help in actualization of its mission. Efficiency is the cost of production which should be less than the input cost introduced into the system (Machuki & Aosa, 2011). Financial health refers to capability of an organization to generate sufficient revenues to meet its operating costs, manage debts and allow for growth while maintaining service levels. Further IDRC (1999) indicated that for financial viability to occur in an organization the cash flows into the organization must be greater than the cash outflows. IDRC (1999) continues to argue that conditions attached to financial health include multiple funding, positive cash inflows and financial surplus.

Organizational performance is the measure of standards and indictors of effectiveness, efficiency and environmental responsibility which includes productivity, waste reduction and regulatory compliance either qualitatively or quantitatively. (Maharm & Anderson, 2008). Companies must identify their relevant indicators of performance, their relation to company goals and performed activities. Measuring firm performance can be done by use of accounting ratios such as return on assets, return on capital employed as well as return on equity (Maharm & Anderson, 2008).

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### 1.1.3 Corporate Governance and Performance

Performance of an organization is usually affected by corporate governance. Organization for Economic Cooperation and Development (OECD) states that the extent to which corporations comply with the basic principles of good corporate governance is vital in investment decisions as it relates to the increased accessibility to international resources which are necessary for investment. The international flow of resources enables the companies to access financing from a larger pool of investors (OECD, 2011). Thus corporate governance practices employed in a firm must be well defined and comprehended so that organizations can reap benefits of international and domestic funding which they can invest and improve their performance.

Samia and Salem (2016) asserts that organizations operate in a turbulent economic environment where they strive to achieve in terms of how corporate issues are handled, competitiveness and grow in market share which is key in improving the corporate image. Corporate governance is a conception that relates to the way in which resources within a corporate entity are prudently consumed to achieve overall company objectives, it keeps the organization in business and creates a greater prospect for future opportunities (Kajola, 2008). As the believe goes, organizations that have embraced good corporate governance should perform better than those which are governed poorly. In this regard, a lot of interest have been accorded to the topic of corporate governance and its effects on organizational performance. This can be attributed to the fact that the structure of governance in an organization affects its ability to respond to its external environment hence affects its performance. Thus, good corporate governance is essential for any organization (Claessens & Yurtoglu, 2013). Furthermore, good corporate governance structure benefits the organization in easily accessing cheap financing thus increasing its performance.

The relationship between corporate governance and performance is manifested in the various dimensions of good governance. It is widely believed that the performance of an organization is enhanced by good corporate governance that exist therein (Braga, Alves & Shartri, 2011; Eichholtz & Kok, 2011). It ensures compliance with existing legal framework so as to protect shareholders from fraud of organizational failure.

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With proper governance mechanisms in place which include a board that directs and controls the management, then the managers will not pursue their own interests which leads to improved performance of organization (Gachoki & Rotich, 2013). Therefore, good corporate governance curtails the possibility of poor performance and failure of an organization.

Kombo, Chepkoech, Koech and Shavulimo (2014) agrees that corporate governance promotes reduction of waste on non-productive activities which diverts the organizations assets and cash flows. These activities include shrinking, excessive remuneration by the management, perquisites and asset-stripping. Furthermore, existence of good corporate governance practices lowers the agency costs due to better shareholders protection which results in superior willingness to accept lower returns on their investment. This renders the organization to become more attractive to external financiers in direct proportion to arise in their corporate governance profile (Kombo *et al.,* 2014). Further, managers become less susceptible to making risky investment decisions and are able to focus more on maximizing value of projects that promotes efficiency. As expressed by Love (2011) the benefits of corporate governance are ultimately increased cash flows and high-ranked performance of the firm.

### 1.1.4 Water Service Providers in Kenya

Water has always contributed to the growth of economy of a country. Water supply and sanitation in Kenya has witnessed major reforms since 1990s. During this time, it became clear that previous targets by the government could not be achieved. The sector performance in Kenya faced a downward performance attributed to poor management of the utilities, malpractices in management of funds and unparalleled growth in demand for these essential services. This led to crisis in public health and other public services which served as an impetus for change. Pressure for the services was expressed through formal complaints procedures and the media (World Bank, 2010).

The institutional reforms that were brought about following the enactment of the water act 2002 were done to minimize duplication and maximize efficiency. The water service providers (WSPs) were mandated to develop and provide services.

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These changes were expected to remedy the poor provision of water and sanitation through commercialization of the publicly owned utilities to private entities as stipulated in the companies Act (Cap 486) of the laws of Kenya (Water Act, 2002). This followed the defining of the national water services strategy as stipulated in sections 49 and 50 of the water act 2002.

The National Water Services Strategy (NWSS) was prepared to address water supply crisis which cannot be overstressed. It provided for a clear, accountable and transparent roadmap to achieve the vision of assured water supply, sewerage and on-site sanitation services for all Kenyans for improved health and job and wealth creation (NWSS, 2007). The main objectives of the strategy are to ensure that water provision is available at all times as well as strategize and formulate a program that will continue to extend sewerage services to the entire population. It defines the process of ensuring that all areas have sufficient water and sewerage services and that service providers are available for provision of the essential services (EIA, 2007).

Water Services Providers (WSPs) are business entities established and mandated to retail water and sewerage services to consumers. As an entity, the provider has to register with Water Services Regulatory Board (WASREB) and be licensed by the respective Water Service Board (WSB) for it to operate. Most of these service providers were initially owned by the local authorities, municipal and town councils, which have since been subsumed by the county governments.

Water service provider is defined as a company, non-governmental organization or any person providing water services in accordance with an agreement between the party and the licensee, the water service boards (Water Act, 2002). The main responsibilities of a water service provider are service levels, billing and collection of revenues for the company operations. The Water Service Providers (WSPs) are expected to operate with maximum efficiency in the provision of services as well as ensure satisfaction and protection of all water consumers, taking into account equity and sustainability (WASREB Guidelines, 2003). Embracing practices of good corporate governance as stipulated in the guidelines will lead to improved performance.

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### 1.1.5 Machakos Water and Sewerage Company

The company was established in 2005 under the companies Act Cap. 486 of the Laws of Kenya) as a private company. The Company is mandated to provide safe water and sewerage facilities on a commercial basis and is responsible for water supply within the Machakos municipality in Machakos County. It works under TAWSB, which came into existence on June 4, 2008. The company was declared under a gazette notice No 69 as contained in the Kenya Gazette Supplement No 25. The company became the eighth WSP under TAWSB mandated to provide portable clean and safe drinking water to the residents of Machakos town and its environs. It was licensed as WSP by WASREB on 1st September, 2008.

The governance and leadership of the company is entrusted to the board of directors. It has optimal board membership of nine (9), which is well representative with good gender representation where one third of the directors are women. The board is drawn from various stakeholders with representation from Machakos County Government, Non-governmental Organizations, Business Community, Religious Institutions and People with disability. The company underscores the value of enhancing transparency in the management and accountability of public resources (WASREB, 2007). Good governance is ascertained through various committees which are Audit, Finance and General Purpose, and Technical and Monitoring committees and Full Board as per guidelines by WASREB. The committees and board meetings are held once after every three months hence a total of four meetings in a financial year as stipulated in the guidelines WASREB, 2003).

Machakos Water and Sewerage Company (MACHWASCO) has a specific Service Provision Agreement (SPA) with TAWSB mandating the company to ensure sustainable supply of adequate and quality water services with affordable tariffs, maintenance and improvement of water and sewerage infrastructure. The dire need for good governance is critical due to the growing need of transparency and accountability of MACHWASCO from the government, stakeholders and owners. Good corporate governance practices will lead to improved performance and customer satisfaction (SPA, 2013).

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## 1.2 Statement of the Problem

Corporate governance practices have continued to weaken in Kenya despite the existence of tight regulatory framework (Pletzer *et al.*, 2015). Many corporations have been faced with major scams affecting the corporate end of the organization. The directors are being accused of acting in illegality and irregularities management of the organizations. The government has cited poor corporate governance in state corporations as a key threats towards achieving Vision 2030. While it is the desire of every organization in today's modern corporate world to improve its performance, the issues on effects of corporate governance and performance of organizations remains a hot topic of research (Guzeh, 2012).

Commercialization of the Water Service Providers (WSP) led to separation of ownership and control which instigates conflicts between the management and board of directors. The board of directors represents the shareholders. Shareholders are more concerned in value maximization of the company while managers are inclined to focus more on their perks and job security. In MACHWASCO, the performance has been fluctuating making it difficult for the company to deliver the services as expected and operate at the required minimum service levels (WASREB Impact Report, 2015). It is possible to attribute the fluctuation in performance to corporate governance practices in the water sector. Efforts should be geared towards remedying the situation else there are likely to be failures and malfunctions making the company unsustainable.

Fondo (2016) studied on effects of corporate governance on financial performance of state owned corporations in the service industry in Kenya using a sample of 50 state owned corporations under the service industry who had offices in Nairobi. The study's findings revealed that poor performance of organizations is attributed to poor corporate governance practices which further leads to poor management of financial resources and inefficiencies. Kiratu and Moronge (2016) noted a positive correlation between corporate governance and performance in their study on influence of corporate governance on organizational performance in Kenya focussing on Agricultural State Corporations.

Furthermore, extant literature (Guzeh, 2012; Ndung'u, 2013) has identified corporate



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governance as key in the performance of a company. These studies recommended that companies should beef-up their governance structures if they are to remain financially sustainable. Ng'etich (2015) investigated on the effect of corporate governance and the financial performance of state owned corporations focusing on the water companies in Kenya. Research on corporate governance practices has been limited to state owned corporations without giving much attention to the specific water service providers. Most of these studies have focussed on financial performance and little has been done to address the general performance of organizations. Thus there is a missing link on how corporate governance impacts on the general performance which is vital for sustainability and growth of an organization. This study therefore, sought to establish the influence of corporate governance on performance of Machakos Water and Sewerage Company.

## 1.3 Research Objectives

### 1.3.1 General Objectives

The general objective of this study was to investigate the influence of corporate governance on performance of Machakos Water and Sewerage Company Limited.

### 1.3.2 Specific Objectives

The specific objectives of this study were:

i. To establish the influence of board structure on performance of Machakos Water and Sewerage Company Limited.
ii. To determine the effect of strategic roles of the board on performance of Machakos Water and Sewerage Company Limited.
iii. To examine the influence of corporate leadership on performance of Machakos Water and Sewerage Company Limited.
iv. To investigate the influence of board independence on performance of Machakos Water and Sewerage Company Limited.

## 1.4 Research Questions

The study sought to respond to the following research questions;

i. What is the influence of board structure on performance of Machakos Water and Sewerage Company Limited?

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ii. How does the strategic roles of the board influence performance of Machakos Water and Sewerage Company Limited?
iii. What is the influence of corporate leadership on performance Machakos Water and Sewerage Company Limited?
iv. How does board independence influence performance of Machakos Water and Sewerage Company Limited?

### 1.5 Scope of the Study

The study focused on the influence of corporate governance on performance of water service providers. The independent variable for this study was corporate governance which was measured using board structure, board strategies, corporate leadership and board independence. The dependent variable was performance which was measured using customer satisfaction, growth in area of coverage, reduction in non-revenue water, growth in revenue and improved service delivery. The unit of analysis was delimited to Machakos Water and Sewerage Company in Machakos County, whereas the unit of observation comprised of the top level management, middle level management, supervisors and unionisable staff. The study was conducted in the period between March and May, 2018.

### 1.6 Significance of the Study

Policymakers would benefit from this study as the findings provide a basis for establishing the relationship between corporate governance and performance of the water company. It also provides basis for understanding the influence of various corporate governance practices and how these practices impact on performance. These findings would be relevant in providing value added information which will be key to policy formulation in the water companies. The regulator, WASREB would be able to appreciate the role of corporate governance on performance hence develop mechanisms of monitoring the performance of the board and follow up on implementation of corporate governance guidelines by water service providers.

Management of Machakos Water and Sewerage Company would benefit from this study as the findings would be used to draw inferences on practices of corporate governance and how they impact on performance. Therefore, the management can

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devise ways of promoting good governance. Further, the management can use the findings as action plans that would help in enhancing better performance hence efficiency and effectiveness in service delivery.

Management of other water service providers would benefit from this study as the findings would intensify the pool of knowledge on the contribution of corporate governance practices in improving efficiency and effectiveness of the organization. This would result in above average performance of the water companies.

Furthermore, scholars and academicians would benefit from this study as the findings would add to the existing body of empirical literature. In addition, the study would serve as a springboard for future researches that are of imperative nature and those that will involve embraced conceptualization through use of intervening and moderating variables.

### 1.7 Limitation of the Study

The researcher experienced some levels of difficult in accessing the target respondents due to the nature of their positions in the organization. This limitation was mitigated through placing appointments with the concerned respondents via human resource department and seeking their consent. The researcher faced challenges as a result of sensitive and strategic nature of some information required for the study where respondents were not willing to give objective and honest data for fear of victimization. Nevertheless, this challenge was mitigated by assuring the respondents of confidentiality in handling collected data. This was upheld through use of codes in place of the respondents' identity. The researcher also used research permit letter from the National Commission for Science, Technology and Innovation (NAC OSTI) as assurance that data collected is for academic purposes only.

### 1.8 Assumptions of the Study

In this study, the researcher assumed that the respondents would be readily available and that they would corporate in filling-in the questionnaire. The researcher also assumed that the respondents would give an honest information which will help in giving an insight of how corporate governance influences the performance of the water service provider as employed in Machakos water and sewerage company. Further, this study was based on the assumption that the respondents were well versed

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and understand the corporate governance practices employed in the organization and how they impact on performance of the company.

# CHAPTER TWO
# LITERATURE REVIEW

## 2.1 Introduction

The chapter focusses on reviewing what various scholars and authors said in their past studies in the same field of study. The literature review will look at theoretical and empirical framework that will form the basis of the study and enable the researcher to ascertain major variables.

## 2.2 Theoretical Review

### 2.2.1 Agency Theory

The concept of agency was first discussed by Berle and Means (1932) who argued that there is a need to separate ownership and control of organizations. They indicated that it could be a source of conflicts. It became widely accepted after the formulation of agency problems in governance of the firms by Jensen and Meckling (1976). The model of agency theory expounds on how the principal and the agents relate (Katheen, 1988). According to Jensen and Meckling (1976), managers are likely to pursue their own interests and are opportunistic. As such, this raises a prospect that the executive, the agent, might be inclined to work towards their personal interests rather than those of the owners of the business, the principal. As a result conflicts arise creating an agency problem. Himmelberg (1999) says that agency problem results when there is laxity in the supervision of the managers activities by the owners of the organization who are the shareholders.

Green (2008), argued that ownership and control in a large organization is often seen as a way of creating power base for executive, which is the management. This is so because the critical information is available to managers who are delegated to run the

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organization and this can make them act in a manner which will give them undue gain at the expense of stakeholder's interests. It is also grounded on the fact that people have self-interests instead of being self-sacrificing hence may not act honestly in the best interest of others as they seek to maximize their own utility (Opanga, 2013). Further, Daily, Dalton & Canella (2003) indicated that the effectiveness of this theory is limited by the fact that it is conceptually simple and reduces the corporation into two parties' i.e managers and shareholders. Secondly, the theory suggests that employees and managers in organizations can be self-seeking. Generally, managers are expected to act in a way that maximizes the wealth which is the best interest of the owners of the business which may not happen since they pursue their own interests.

The proponents of this theory consider the board of directors as the guardians of the shareholders' interests. According to them, corporate governance is meant to check on the perceived conflicts between principal and agent, (Mallin, 2010). The agency problems can be countered. Jensen (1983) suggests that the firm can put in place internal systems designed to operate efficiently and monitored all through the institutional framework. Performance contracts may be introduced between the owners and the managers.

This theory is used to understand how the principals and agents relate. The principal denotes the owners of an organization which include the shareholders while the agent includes the management who are hired to perform work on behalf of the principals. In this theory, managers are believed to act in the best interest of the owners of the organization. Thus, they put more effort in maximizing the wealth of the shareholders (Clarke, 2004).

This study sought to identify the link between corporate governance and performance. Under the theory of agency, the board members are appointees of the organizations ownership to oversee their mandate in the operations of the organization. Consequently the management is contracted by the owners to run the day to day running of the organization. This theory therefore helped to understand how board structure influences performance of organizations. Further it provided a deep insight on independence of the board and control of organizations as employed in Machakos

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Water and Sewerage Company, and their effect on the expectations of each party without compromising each other's interests.

### 2.2.2 Stewardship Theory

Stewardship theory was first put forward by Donaldson and Davis (1993) where they highlighted on the existing relationship between ownership of a company and how it is managed. The theory elaborates on the relationship between business owners called the principals and the stewards who are the managers. The steward is expected to protect and maximizing the wealth of the principal through performance (Davis, Schoorman & Donaldson, 1997). By so doing, the functions of a firm are maximized (Davis, *et al*, 1997). Further Davis *et al.*, (1997) urged that stewards should work for the best interest to benefit the principal and the organization. Therefore, the relationship existing amongst the principal and steward, the environment and epitomes of a firm helps to build the stewardship behaviour.

Donaldson and Davis (1994) asserted that under stewardship theory, managers are good stewards who work diligently to realise high levels of profit and returns for the shareholders in an organization. Furthermore, Guzeh (2012) indicated that corporate executive and managers are seen as stewards who work, protect and make profit for the shareholders. Therefore, they work diligently, are responsible and honest so as to satisfy the interests of the company and its shareholders. This theory argues that managers are mainly accountable for the success or failure of a company and expect stern consequences in case of failure and will receive bonuses and other benefits when the business succeeds. Thus, they need freedom in decision making other than being constrained due to control by external directors which may hinder their optimum productivity.

According to Clarke (2004), for managers to be successful in their quest for wealth maximization, the position of the CEO and chairman of the board must be held by one person. This convergence of roles ensures that power and authority is vested in one person such that employees clearly understand their boss. Unifying the role CEO and chairman will help reduce agency costs and have greater role as stewards in the organization to safeguard the interest of owners (Daily *et al.*, 2003).

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Stewardship theory as used in this study helped to give a deeper insight on inclined roles of independent directors and executives to run the organization to maximum performance while meeting the interests of the shareholders of Machakos Water and Sewerage Company. Further it would help understand the corporate leadership and independence of the directors and hence extrapolate that managers are contracted with a prime motive of generating wealth to the shareholders and there is consequences for performance.

### 2.2.3 Stakeholders Theory

Stakeholder theory was attached to the discipline of management in the 1970's. Stakeholder theory states that many people have a stake in a firm beyond the shareholders and management. The theory was developed by Freeman (1999), where he identified a stakeholder as any group or individual who can affect or is affected by decisions, objectives and achievements of an organization. Just as in agency theory, managers in stakeholder theory work for the stakeholders and there is a network of relationships between the managers and stakeholders in an organization (Freeman, 1999). Organizations that endeavour to meet expectations and interests of a diverse group of stakeholders creates value over time (Freeman, 1984; Freeman, Harrison & Wicks, 2009). They desire that there needs are met and that they benefit from the operations of a firm. The stakeholder's theory is derived from both sociological and organizational disciplines. It is a theory that combines philosophy, ethics, political theory, economics, law and organizational science (Wheeler *et al.*, 2002). Further, Clarkson (1994) expressed that the stakeholder's theory asserts that a firm is a structure in which stakeholders operate in a much wider structure of the host society.

Stakeholder theory examines the organization in a range of implicit and explicit constituents (Jones & Politt, 2002). Stakeholders are diverse and, either affect or affected by the operations of the organizations. According to Freeman (1984), all stakeholders are customers who can make decisions regarding the operations of an organization and state whether they are served to their expectations. Thus, an organization that strives to make its stakeholders satisfied will retain their support and participation and hence improvement in performance. Further, managers should treat

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the stakeholders well and work towards meeting their expectations and interests for better performance.

Performance of an organization is a sum total of many factors presented by the environment to the organization. The organization usually has high level of influence on its entire internal environment unlike to its external environment. Stakeholders are interested parties to the operations of the organization presented by the external environment. They have vested interests on the operations of the organization until their interests are met. Therefore, this theory helped in understanding organizational stakeholders, their roles, and interests and how these interest are met without affecting the overall performance of an organization. Hence it helped in highlighting the independence of boards in decision making and strategies adopted by the board to meet the interests of the stakeholders.

### 2.2.4 Resource Dependency Theory

This concept was first crafted Pfeffer and Salancik (1978). They helped to appreciate the behaviour of an organization by considering the environment within which it operates. They urged that an organization is an open system that depends on contingencies in its external environment. The theory recognizes the external factors to an organization are those which influences its operations. Managers are thus expected to act to reduce effects of environmental dynamism and uncertainty through devising ways to respond to the changes (Hillman, Withers, & Collins, (2009).

Hillman, Canella, and Paetzold (2000) asserts that RBT emphasizes on the role played by the board in providing essential resources to an organization through their linkages to the external environment. It provides a focus on the involvement of independent representatives in the organization who act as a link between the organization and its environment, and as a means of accessing resources that are critical to the organization. Furthermore, it elaborates on how firms can achieve competitive advantage through responding to the uncertainties as well as sustainability (Pearce *et al.*, 2012). An organization should possess unique resources that help them to remain competitive hence greater performance.

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Resource dependency theory puts forward that organizations can be considered as having resources which are heterogeneous in distribution throughout the firm and they persist over time. Hamid (2011) asserts that factors including scarcity of resources are important and the extent of concentration of the resources appear to intensify the push for the dependency. Furthermore, Penrose (1959) argues that there exist a slack in resources possessed by a firm. The resource slack, which is the difference between the resources that are owned by a firm and those that are required by the current business, acts as a channel of growth. Organizations may possess the same resources but have different demand for these resources in their current business Mishina, Pollock & Porac, 2004). Thus, this difference leads to further growth since the firm is able to take advantage of the opportunities presented in the environment (Mishina *et al.*, 2004).

Pfeffer and Salancik (1978) outline that it is the mandate of the directors to adopt resources that play a critical role in ensuring that the organization survives the turbulent and uncertain business environment. RBT seeks to solve the challenges of scarce resources by ensuring that a firm has external linkages with the resources in the environment in which it operates. According to Tokuda (2005), scholars have failed to support how the structure and performance of an organization relates. Thus, the internal environment should be considered as well. Resource dependency theory emerged as a key theory in strategic management since mid-1980s (Pearce *et al.*, 2012). However, some scholars argue that it does not empirically meet the content criteria for a theoretical system (Priem & Butler 2001).

For any organization to prevail, it must have a proper combination of its resources. These resources can either be human or non-human resources. Combination of these resources for optimal use and output has a great effect on the overall performance of a firm. Directors source for information and skills, formulate policies and legitimacy that help respond to the uncertainties in the environment. RBT was relevant to this study in that it focuses on board cohesiveness, independence, board diversity and strategies that help link with the environment towards realization of the key objectives.

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## 2.3 Components of Corporate Governance

The major components of corporate governance practices in firms and which this study will seek to focus on include board structure, corporate leadership, corporate strategic roles and board independence.

### 2.3.1 Board Structure

According to Samia and Salem (2016), corporate governance structures are defined as the systems or mechanisms that are put in place to monitor managers and improve transparency in an organization. Organizations with different performance adopt different structures. This study will look at the board size, board diversity and frequency of board meetings. According to Aggarwal, (2013), the board size constitutes of the number executive and non-executive directors in a particular board. The size of the board has a noticeable effect on the overall organizational performance. Further, the size of the board may give conflicting results. It has been argued by many scholars whether it is a large or small board that is more effective. This is seen in a review of the work of (Kiratu & Moronge, 2016) who argues that large boardrooms slows the process of decision-making thereby impeding change implementation. Furthermore, Adams and Mehran (2012) asserts that larger boards indicates complexity of a structure existing in a firm.

The concept of board diversity and organization performance is unavoidable. Diversity refers to social attributes which can either be primary or secondary attributes. Primary categories of diversity include age, race, ethnicity and gender. The main categories of diversity are age, ethnicity and gender which provides a link between board diversity and organizational performance (Adams & Mehran, 2012). It is assumed that member with obvious differences will bring along different ways of thinking as part of their identity. Interest in executive diversity has been urged by many scholars. The frequency of board meetings leads to increased level of corporate performance since the board allocates adequate time to discuss and make effective decision (Samia & Salem, 2016).

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### 2.3.2 Corporate Leadership

Board leadership signifies the manner in which the board provides direction, implementing plans, policy formulation and motivating staff to get work done. It is the influence and legitimate authority acquired by the leader so as to effectively transform an organization through directing resources towards achieving a desired goal. Leadership styles of the board therefore should be carefully selected and to guide and motivate subordinates (Kibiwott, 2014).

Corporate leadership on the other hand looks at the separation of office commonly referred to as CEO duality. CEO duality refers to the separation and or tying of the responsibilities of the chief executive officer with those of the chairman of the board. Aggarwal (2013) stated when the responsibilities of the CEO and chairman are bestowed in one individual, then conflict of interest, concentration of power and board independence will be realised. One of the major roles of a leader is be a source of motivation.

Leadership is key to making people work enthusiastically. The chairman of the board plays a major role in corporate leadership towards moving the agenda of the board forward. Cole (2012) defines leadership style as a particular behaviour a leader displays which have a direct impact on an individual or collective workforce output. The board in an organization dictates the formulation of policies which serve as the guiding principles for day to day operations of the organization. If these policies are deemed to be positive and binding or otherwise, can be source of motivation and or demotivation of the workforce (Aggarwal, 2013). As identified by Muriuki, Cheruiyot and Komen (2017), board leadership is essential in discharging the mandate hence board members must have knowledge and experience.

### 2.3.3 Strategic Roles of the Board

The board constitute the topmost echelon of management of any institution. According to Robinson (2005), strategic planning is a management process used to prioritize, focus energy and resources, and making sure that human resources and other stakeholders within the organization are all working towards achieving a common goal. Strategies are efforts that produce vital decisions towards shaping and guiding an organization to success. Effective strategic planning articulates the

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direction of an organization and the actions that are paramount in making progress as well as understanding the success. As a result of this activity a strategic plan is born which is used to communicate the organizational goals, and how to achieve them. It gives a futuristic approach of what an organization seeks to achieve in a certain time frame and within a limited constraint of resources (Robinson 2005).

The board is also charged with the responsibility of performance management within an organization. To ensure proper management of performance, employment is based on contracts whereby the employee and the employer agrees on the minimum terms of engagement in terms of inputs and outputs. To gauge the performance of managers a performance Contracting has become a common practice. This performance contract is a tool used in measuring actual output in terms of performance usually compared against set targets. These targets are usually negotiated and agreed upon between the employee and the management. It gives the performance commitments, accountabilities and responsibilities of the two parties.

### 2.3.4 Board Independence

The performance of an organization is largely affected by the independence of the board on decision making. Interested parties always try to have their way in influencing the decision of the board in a bid to attain their personalized interests. To enhance these independence board members ought to be both independent non-executive members and executive members (Ngetich, 2015). The executive representation in the board is by the chief executive director whose prime purpose in to oversee the implementation of the strategies as agreed by the board. Aggarwal (2013) states that independency the board serves a very critical role in monitoring and evaluation of company's management. Thomsen and Conyon (2012) argue that if the board comprises of members who have executive rights, they are likely to accept all dissertations that are put forward thus affecting the quality of decisions made.

The independence of the board is also indicated through the audit committees which gives independent audit reports. According to Guzeh (2012), both the board of directors and the audit committee should be independent from the management. This enhances reporting systems within the organization, and quality of the financial reports generated since they are not subject to potential conflicts of interest. Further, Aggarwal (2013) added that, the increase in highly ranked corporate scams has

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increased the need for organizations to have a robust and effective audit committee to give dependable reports. The frequency of the board meetings and the level of independency of the audit committees are vital in ensuring credible audit reports.

### 2.4 Performance

Performance refers to the end results of the organization's operations and activities. According to Machuki and Aosa (2011), performance of an organization is reflected in its achievements based on a set criteria. An organization is a voluntary association of resources that are used in production. These resources include human resources and financial resources which are aimed at achieving a defined and shared vision.

Organizational performance can be measured using financial indicators, effectiveness and efficiency in service delivery against set targets (Machuki & Aosa 2011). Performance can also be measured using Balanced scorecard (BSC) relies on combination of measures in evaluating organizational performance (Kaplan & Norton, 1992). Further, they assert that various measures of performance should be multidimensional in nature such that they cover both financial and non-financial measures. This helps improve the performance of a firm. Kaplan and Norton, (1993) assert that using balanced scorecard, each unit in a firm develops its own specific measures that capture their own strategies while linking it to the overall vision and strategy.

Measurement and analysing organizational performance is a key factor in achievement of organizational goals (Kiratu and Moronge, 2016). Performance of organization is the realization of tasks or goals to a certain level of desired satisfaction. According to Venkatraman and Ramanujam (1986), various approaches are used to measure organizational performance. They proposed three general levels of organizational performance. The first approach is financial perspective which focuses on financial results. Measures on financial performance include return on investment (ROI), reserves and growth in realized revenues. Further, they proposed the market related approach which includes market share and growth. The third approach is based on measure of organizational effectiveness which is closely related to stakeholders other than the shareholders. These stakeholders include employee

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satisfaction, quality of service delivery as perceived by customers as well as customer satisfaction.

Organizational effectiveness is a construct that is grounded in the values and preferences of evaluators (Cameron, 2015).The employee attitudes and behaviour influences business outcomes. Employee satisfaction has an impact on profitability and customer satisfaction which affects the performance of an organization (Kiratu & Moronge, 2016). In this study, customer satisfaction, growth in area of coverage, reduction in non-revenue water, growth in revenue and improved service delivery will be used to measure performance of the water company.

## 2.5 Empirical Literature Review

### 2.5.1 Board Structure and Performance

A deep analysis on the empirical evidence on the topic of study is mixed. A study conducted by Miring'u and Muoria (2011) on the effects of corporate governance on performance in Kenyan state corporations indicated that corporate governance has a direct effect on the financial performance of a corporation. The study was descriptive with a sample size of 30 corporations. The study focussed on financial performance, board size and composition. The findings of the study revealed that there exist a positive relationship between the financial performance, which was measured using return on equity (ROE), and board composition of all state corporations. Therefore, if a board has many people who have diverse backgrounds, it is expected that they bring diversified knowledge and expertise to the board. Nevertheless, the study failed to integrate the optimal board size that would not compromise decision making as well as be effective in enhancing performance of the organization.

Bermig and Frick (2010) analysed the effect supervisory board size and composition on the evaluation of Germany firms using 294 companies while controlling for a large number of other potential determinants of the firm performance. The conclusion of the study showed inconsistencies on how board size affected the performance of the firm. Ujunwa (2012) investigated on the impact of corporate board characteristics on financial performance of Nigerian quoted firms. The board characteristics considered in the study were board size, board skill, board nationality, board gender, board

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ethnicity and CEO duality. The findings of the study showed a negative linkage between board size and gender diversity. Nevertheless, these results are inconsistent to the extent that all board characteristics are found to have an impact on performance.

Opanga (2013) established that the number of board committees, board meetings frequency and number of board of directors has a positive correlation with financial performance. He urged that each of those variables of corporate governance played a vital role on performance of the insurance company. In his study on relationship between board composition and financial performance of listed firms at the Nairobi Securities Exchange, Wetukha (2013) established a positive relationship between board size, board independence and CEO duality. However, gender diversity and proportion of non-executive directors had no effect on performance.

### 2.5.2 Strategic Roles of the Board and Performance

Tuwey and Tarus (2016) looked at the relationship between board leadership and board strategic involvement in private firms in Kenya. Further the study sought to explain how to moderate CEOs power looking at 186 CEOs. The findings showed that board chairman's leadership efficacy and board members' personal motivation had a positive effect on board strategic involvement hence performance. Hyvari (2016) investigated on the roles of top management in the effective company strategy implementation. The findings of the study revealed that corporate the board distributes rights and responsibilities among different participants in the organization, and is responsible for monitoring, control and directing which impacts on the performance and implementation of projects. The study revealed that there is interconnection between the company strategy implementation, corporate governance and project. Furthermore, the study recommended that clear roles and responsibilities in the organization should be defined and communicated well, and that the board should monitor implementation and performance of strategies, projects and policies. However, the study used case study hence qualitative data. Thus the findings could not be generalised.

Atieno (2012) carried a study on the relationship between board monitoring and performance of the companies listed in Nairobi Securities Exchange, the study



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focused on investigating the effects of board monitoring through qualitative measures of firm's board of directors and its financial performance using ROA. The findings revealed a positive correlation between board monitoring variables and performance. Nevertheless, the study used casual analytical design and relied on secondary data which could not be used to give inferences on future performance.

Various studies have been conducted by scholars on how the number of board and performance of a firm relate. Yoshikawa and McGuire (2008) stated that an increase in the number of directors increases the pool of expertise available in a firm therefore large board sizes are likely to have more knowledge and skills compared to smaller boards. In contrast, Jensen (2009) argued that increase in board size leads to decrease in its ability to monitor firm's performance due to increase decision making time. This asserts therefore that larger board rooms weakens a firm performance thus larger boards are likely to weaken the firm performance as the board will be less effective in substantive discussion of major issues among directors.

Fondo (2016) in his study on the effect of corporate governance on financial performance of state owned corporations in the service industry in Kenya found that there is a positive correlation between corporate governance and financial performance of the state owned corporations using return on assets to measure financial performance. Thus embracing good corporate governance practices enhances financial performance of state owned corporations. Ng'etich (2015) studied on corporate governance and financial performance of water companies in Kenya. The findings of the study revealed a positive correlation between financial performance and corporate governance.

### 2.5.3 Corporate Leadership and Performance

Rutledge and Karim (2016) using proportion of independent directors, board interlock and committee overlap to measure effects of board independence and CEO duality on firm performance revealed that CEO duality had no relationship with performance. However, in its composite nature, CEO duality where the role of CEO and chairman are not separated has an impact on performance since decision making resides with one person. The study used secondary data from annual financial reports and BoardEx

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database. The findings of the study cannot be used to give future performance as it relied mostly on past data.

Analysing the impact of corporate governance on firm performance in Bahrain stock exchange, Ahmed and Hamdan (2015) found that the board of directors were not controlled by a large number of independent directors. Further, they established that the position of the CEO and chairman were split as the chairman was an independent director. This is in line with good corporate leadership structure as the chairman has a great power for independent decision making of the board. However, the study used secondary data and therefore the findings could not be generalised.

Wanjiku (2011) undertook a study to assert how corporate governance practices relate to growth of companies listed in the Nairobi Securities Exchange. The study looked at issues like corporate communication, leadership, and technology application. The findings of the study revealed a positive linear relation on corporate governance and growth in those companies. Mang'unyi (2011) explored the relationship between ownership structure and firms performance studying banks in Kenya. The findings of the study revealed that there was a significant difference between corporate governance and financial performance of the banks. He recommended that corporate entities should embrace good corporate governance practices so as to realise positive performance for the investors. The regulatory agencies including the government should promote and socialize corporate governance and its relationship to organization performance across organization.

### 2.5.4 Board Independence and Performance

Gachoki and Rotich (2013) using purposive sampling technique to establish the influence of corporate governance on the performance of public organizations in Kenya concluded that board composition had a more influence on performance. Board composition was measured in terms of the composition of insider and outsider directors in the board. It also factored the political and professionals present in the board. The results showed that control of the board by outsiders supported performance of the organization. They recommended that enforcement measures on corporate governance should be laid down by the government so as to enhance compliance by public organizations. However, use purposive sampling technique

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meant vulnerability to errors in judgement by the researchers and low level of reliability hence the findings of the study could not be generalized.

Sala (2011) conducted a case study to establish the corporate governance practices at the Kenya National Library Services. Using audit committee, finance committee, board nomination committee and code of conduct, the findings of the study revealed that there was no board nomination committee in place and as such board members were appointed through ministerial and presidential appointments. As a result, the independence of the board is not enhanced since decision making was be influenced by the minister. The audit committee was found to be independent and they had the power to seek for explanations, information and understand various accountability relationships. The study concluded that audit committee independence had a direct relationship with the level of performance. However, the study used case study research design and thus, the inherent qualitative data utilized does not support generalization of the findings.

Various studies on the effect of board structure on firm performance revealed either mixed or opposite results to what was expected from the agency cost argument. Some of these studies established that firms whose boards were dominated by outsiders had better (Ravina & Sapienza, 2009) whereas others found that there is no such relationship in terms of accounting profit or firm value (Adams *et al*., 2010). Rezaee (2009) argued that firm performance was insignificantly related to a higher proportion of outsiders on the board and therefore, the relationship between the proportion of external directors and firm performance is mixed. Furthermore, Kyondu (2014) examined the corporate governance effects on performance of SCs in Kenya using descriptive survey design. The findings of the study indicated that corporations that had adopted good corporate practices performed well. The study further recommended that financial monitoring should be done thoroughly by the board and SCs should adopt regular corporate audits and evaluations.

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## 2.6 Summary of Literature Review and Research Gaps

Many studies have been carried out on corporate governance and performance that have been adopted for this study. A critical review of these studies revealed research gaps that necessitated the need for the current study.

Atieno (2012) studied on the relationship between board monitoring and performance of the companies listed in Nairobi Securities Exchange. The findings revealed a positive correlation between board monitoring variables and performance. The study relied on casual analytical design and secondary data which focuses on past performance. This study used primary data which supports drawing of inferences on future performance. Ahmed and Hamdan (2015) conducted a study on corporate governance and firm performance in Bahrain Stock Exchange. The findings of the study established that the position of the CEO and chairman were split which is in line with good corporate leadership structure. However, secondary data was used which cannot be generalized to give future performance of organizations.

Gachoki and Rotich (2013) in their study on influence of corporate governance on performance of public organizations, a case of Kenya Ports Authority, established that board composition had a more influence on performance. Board composition used in the study included the executive and non-executive directors. The study used purposive sampling technique which is subject to errors in judgement and has a high level of biasness. This study focused on stratified random sampling which minimizes on bias hence findings can be generalized.

Water sector in Kenya is a unique service industry since water is a basic need and a right to all as contained in the Constitution 2010. Water in the right amounts and quality is critical to the wellbeing of the nation. Each water company operates in a unique environment and hence encounters unique challenges some of which are specific to a company. Ng'etich (2015) conducted a study on Governance and financial performance of water companies in Kenya. The findings revealed a positive relationship between corporate governance and performance. However, the study focused on financial performance of these companies leaving non-financial indicators which has a significant influence on performance. This study will focus on non-financial indicators such service delivery and growth in area of coverage so as to

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bridge the gap and allow for general drawing of conclusions on influence of corporate governance practices on performance of water companies in Kenya.

### 2.7 Conceptual Framework

Conceptual framework is a basic structure that grounds the abstract blocks which represent the research variables being conceived (Kotler, 2005. The conceptual framework model is developed from the literature review and is presented in figure 2.1.

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**Independent Variable** **Dependent Variable**

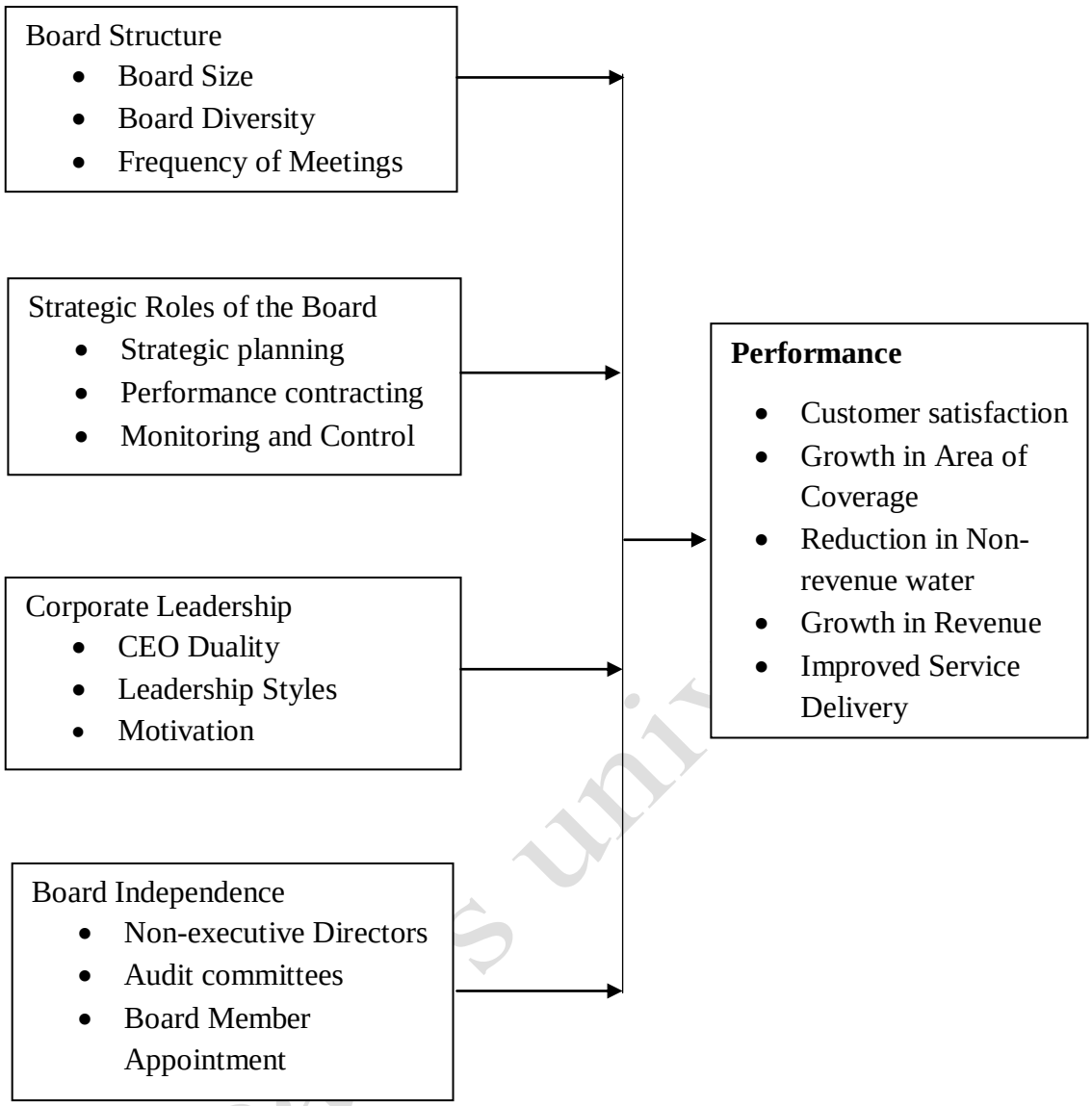



**Figure 2.1: Conceptual Framework**

**Source: Researcher (2017)**

In this study, corporate governance was hypothesized to influence performance of Machakos Water and Sewerage Company. The independent variable of this study was corporate governance while the dependent variable was performance.

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# CHAPTER THREE
# RESEARCH METHODOLOGY

## 3.1 Introduction

This chapter presents the proposed research design, the target population, sampling design, data collection instruments, description of data processing and analysis and the ethical issues in the study. Research design is the procedural plan that is adopted by a researcher so as to answer questions validly, objectively, accurately and economically (Kumar, 2005).

## 3.2 Research Design

This study adopted and utilized descriptive research design as a strategy for integrating the different components of the study in a coherent and logical manner. Descriptive studies often result in formulation of essential principles of knowledge that enables realization of solution to research problems, hence helped to assess the views of MACHWASCO staff on how corporate governance influences performance of the company. The adopted research design helped to explain the relationship among variables and fact finding inquiries of different kinds (Cooper & Schindler, 2005). Descriptive research design was used by the researcher to gather information, summarize, present and interpret it so as to obtain more clarification on issues. This design is of interest to the researcher as it helped focus more on the state of affairs as they exist in the field. The research study was thus able to generalize the findings to the entire population of the study.

Descriptive research helps to ascertain and describe characteristics of variables as they exist in a certain situation (Chandran, 2004). It is used when investigating the current status of a problem (Mugenda & Mugenda, 2003). It is suitable for obtaining systematically factual information of decision making, identify current conditions and opinions thus establish a relationship among variables. Descriptive studies are not only restricted to fact findings, but often result in formulation of important principles of knowledge and solution to significant problems Thus, descriptive design is suitable for this study as it helps the researcher to determine the relationship between the independent variable (corporate governance) and dependent variable (performance of MACHWASCO).

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### 3.3 Target Population

This study was carried at Machakos Water and Sewerage Company Limited in Machakos County. Mugenda and Mugenda (2003) asserts that a target population is the population that is accessible to which the researcher will use to make generalizations of a study. For the purpose of this study, 85 employees of MACHWASCO were considered as the target population. The population was categorised into four functional areas which are; the top managers, middle level managers, supervisors and unionisable staff. The various categories gave an informed decision since each category has a role to play in establishing the influence of corporate governance plays on the performance of the water company.

**Table 3.1: Target Population**

| Category | Frequency | Proportion |
|---|---|---|
| Top Level Managers | 5 | 6% |
| Middle Level Managers | 9 | 10% |
| Supervisors | 12 | 14% |
| Unionisable staff | 59 | 70% |
| **Total** | **85** | **100%** |

**Source: MACHWASCO HRM Department (2018).**

### 3.4 Sample Size and Sampling Procedures

This study adopted stratified random sampling technique where the researcher divided the population into smaller subgroups called strata. Orodho and Kombo (2002) asserts that sampling is process of selecting a number of individuals or objects from a population so that the selected group contains elements that are representative of the entire population.

The researcher divided the entire population into homogenous subgroups. A simple random sample was the taken in each subgroup making it possible to make reliable estimates for each stratum as well as the entire population. This helped to reduce bias in data collected and ensured equal chance of representation across all categories in the company. According to Mugenda and Mugenda (1999) a good sample should be between 10% and 30% of the target population. However, a sample selected for a study should be optimal to fulfil the efficiency, flexibility and reliability requirements

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of a study (Kothari, 2007). As such, this study utilized stratified random sampling and came up with a sample size of 60 respondents as indicated in table 3.2

**Table 3.1: Sample Size**

| Category | Stratum size | Sample size | Proportion |
|---|---|---|---|
| Top Level Managers | 5 | 3 | 60% |
| Middle Level Managers | 9 | 5 | 60% |
| Supervisors | 12 | 9 | 75% |
| Unionisable Staff | 59 | 43 | 74% |
| **Total** | **85** | **60** | **71%** |

**Source: Researcher (2018)**

### 3.5 Type of Data

For the purpose of this study, the researcher used both primary and secondary data. Primary data was obtained from the field while secondary data was collected from research articles, journals, WASREB Impact reports for the period 2012- 2017, unpublished company reports and other publications (Mugenda & Mugenda, 2003).

### 3.6 Data Collection Instruments

This study used questionnaire as the instrument for collecting primary data. The questionnaire was preferred because the respondent were literate and hence able to answer the questions asked adequately. Data collection instruments are tools used to collect information that is critical in proving some facts. The choice of tools used is affected by the nature, purpose and scope of research (Mugenda & Mugenda, 2003).

The questionnaire had both open-ended and closed-ended questions to allow the respondents give relevant answers on the role of corporate governance plays on the performance of the WSP. Further, the respondent will have freedom and convenience of giving their explanations and opinion. According to Kothari (2007), questionnaires are used because the researcher collects information that is of interest to the study and all the respondents responds to the same questions. The questionnaire was administered through “drop and pick” technique.

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The questionnaire comprised of two sections. Section A sought to address the background information about the respondents. Section B has five sub-sections which addressed the general information on board structure, board strategies, corporate leadership, board independence and performance. Secondary data was obtained through review of published documents including Impact reports (2012-2017) published by WASREB on annual Performance review of Kenya's Water Services Sector and records maintained by MACHWASCO.

### 3.6.1 Validity

Validity refers to accuracy and meaningfulness of inferences which are based on the results of a research (Orodho, 2013). It is the degree to which an instrument measures what it purports to measure (Mugenda & Mugenda, 2003). To ensure validity, the questionnaire was discussed with two heads of departments of MACHWASCO and information gathered was incorporated in the content. The questionnaire was also subjected to expert judgement of the supervisors for their opinion and their input was included in the content. Content and construct validity was established through extensive review of relevant theoretical and empirical review. This facilitated the revision and modification of the research instrument thereby enhancing the validity of the questionnaire.

### 3.6.2 Reliability

Reliability of the questionnaire was tested through a pilot study where 10 questionnaires were administered to respondents form the target population. The respondents who participated in the pilot study were excluded from the sample used in the actual study. Kothari and Pal (2007) confirms that reliability is the extent to which data collection instruments yield consistent results under the same circumstances. The questionnaires were collected, coded and analysed for Cronbach's Alpha which was computed using SPSS version 20. This approach is recommended by Cohen, Manion and Morrison, (2007) and it measures the internal consistency and helps to establishes if items within a scale measure the same construct. The overall reliability coefficient was 0.812. Field (2009) observes that Cronbach's Alpha of 0.7 is the threshold for determining reliability of a research instrument. Thus, the aggregate Alpha value of 0.812 was considered adequate.

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### 3.7 Data Collection Procedure

Data collection procedure is essential element in the production of the useful data for analysis. It involves contacting and collection of information from the selected units of study (Cooper & Schindler, 2003). The researcher obtained a research permit from NACOSTI before embarking on data collection. At the company level, permission to collect data was sought from the human resource department of MACHWASCO.

The questionnaires were delivered to all respondents of the study accompanied by a brief introduction letter from the researcher on the purpose of the study. Follow-up through the heads of departments of the respondents was done to enhance response rate. To ensure that all questionnaires administered to the respondents were received, the researcher maintained a questionnaire register. This provided a clear account of questionnaires that were issued and received back. Completed questionnaires were collected at the time agreed with the individual respondents.

### 3.8 Data Analysis and Presentation

The process of data analysis is concerned with bringing order, structure and meaning to collected information (Kombo & Tromp, 2006). In this study, collected data was prepared for statistical where data clean-up was done. This involved editing, coding and tabulation so as to detect any anomalies and check on appropriateness of the responses. Coding was done and specific numerical values were assigned to the responses for further analysis. Completed questionnaires were edited for completeness and consistency (Cooper & Schindler, 2003).

Data was quantitatively analysed using descriptive and inferential statistics. Descriptive analysis was used to summarise data and included frequencies, percentages, mean and standard deviations. Data was then presented using percentage and frequency distribution tables and figures by use of computer Statistical Package for Social Sciences (SPSS) version 20.0. Descriptive statistics provide the basic features of the data collected on the variables under study (Mugenda, 2008).

Inferential statistics was conducted which involved use of multiple regression analysis since there were more than one explanatory variable in this study. This analysis

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helped to establish the relationship between the variables of the study. The regression model was as follows:

$$\mathbf{Y=\beta_0+\beta_1X_1+\beta_2X_2+\beta_3X_3+\beta_4X_4+\varepsilon}$$

Where;

**Y**= Performance of Water Service Provider

$\mathbf{X_1}$ = Board Structure

$\mathbf{X_2}$ = Strategic Roles of the Board

$\mathbf{X_3}$ = Corporate Leadership

$\mathbf{X_4}$ = Board Independence.

$\mathbf{\beta_1, \beta_2, \beta_3}$, and $\beta_4$are regression coefficients to be estimated

$\boldsymbol{\varepsilon}$ = error term

The output of analysis of variance (ANOVA) was used to test whether the overall model is statistically significant by indicating whether or not $R^2$ could have occurred randomly or not. The F-statistic in the ANOVA table was used to measure the goodness of fit of the estimated regression model at 0.05 significance level.

Qualitative data collected from open-ended questions was presented in a narrative form on the basis of common themes inherent from the responses gathered.

### 3.9 Ethical Considerations

Confidentiality and privacy are most key in field research activities as it enhances collection of relevant and appropriate data. The researcher assured the respondents of the purpose of research and maintained confidentiality of the information gathered. Due to the strategic nature of the information collected, the researcher concealed the identity of the respondents so as to uphold confidentiality and enhance protection. In addition the researcher ensured that all authors were acknowledged. A letter of authority to conduct research was obtained from the National Commission for Science, Technology and Innovation (NACOSTI). At the organizational level, the researcher sought permission from the human resource department of MACHWASCO to collect data and obtained an informed consent from individual respondents. Further, the researcher avoided embarrassing and irrelevant questions and language that would make the respondents feel nervous or uncomfortable as noted by Mugenda and Mugenda (2003).

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# CHAPTER FOUR

# RESEARCH FINDINGS AND DISCUSSION

## 4.1 Introduction

This chapter explains on the research findings, analysis, interpretation and presentation. The data was analysed using both quantitative and qualitative analysis. Further, the chapter will discuss the results in line with the theoretical and empirical literature review.

## 4.2 Response Rate

The researcher administered 60 questionnaires out of which 54 were returned. 53 questionnaires were filled-in while one questionnaire was rejected since it was returned unfilled. The analysis of the response rate was as shown 4.2:

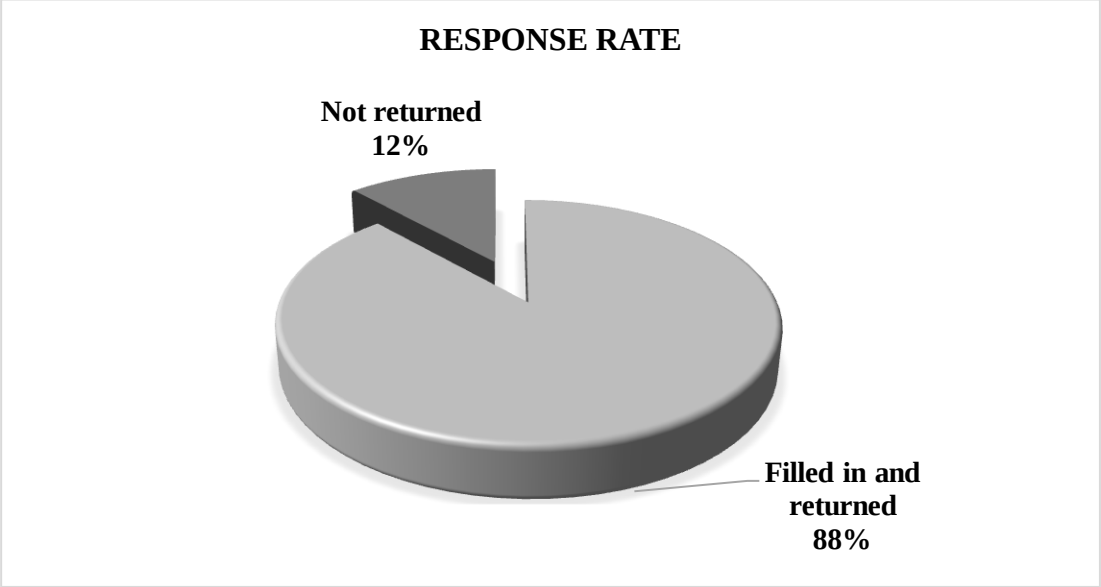



**Figure 4.2: Analysis of Response Rate**

**Source: Survey Data (2018)**

Figure 4.2 indicates that approximately 88% of the administered questionnaires were filled-in and returned. According to Mugenda and Mugenda (2003), a response rate is the percentage of the subjects that respond to questionnaires. Further, a response rate

of 50% is adequate for data analysis and reporting, 60% good and 70% response rate is excellent. However, a response rate of less than 30% is not viable. The excellent response rate was made possible through engagement of research assistants and follow-ups. In this respect, the response rate was considered sufficient for making statistical inference and drawing conclusions.

### 4.3 Background Information

The demographic characteristics of the respondents were analysed on the basis of gender, age, level of education, length of service and level of employment.

#### 4.3.1 Gender of Respondents

The study sought to determine the gender of the respondents. The findings were as presented in figure 4.3:

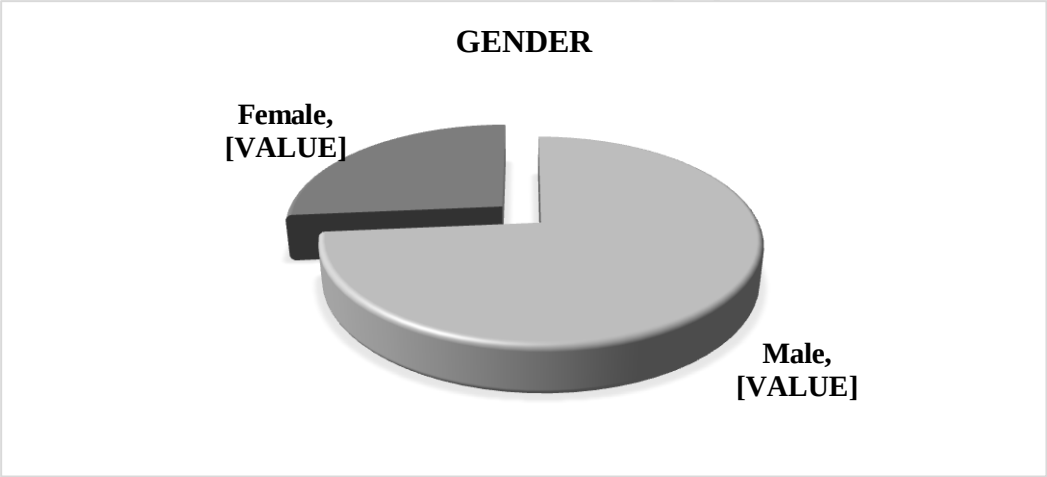



**Figure 4. 3: Gender of Respondents**

**Source: Survey Data (2018)**

According to the findings, out of 53 respondents, 39 (74%) were men whereas 14 (26%) were female. In line with gender mainstreaming, and under the SPA of the Government and its corporations, staff membership establishment in any institution should constitute at least 30% of either gender. The study results therefore revealed a case of gender parity.

### 4.3.2 Age of Respondents

To understand the age of the respondents better, their age was clustered in clusters of 10 years from 20 years to 60 years. Figure 4.4 indicates that majority of the respondents are of the age of 20 to 30 years being 25 (47%) of the respondents, 15(28%) being of the age 30 to 40 year, 8(15%) and 5 (10%) being of the age 41 to 50 years and above 50 years respectively. This is an indication that the company has well planned succession plan. Further, it indicates that the management adopted a well thought strategy to have more young and energetic employees. The age distribution of the population sampled and studied is however fit to draw inferences and conclusions.

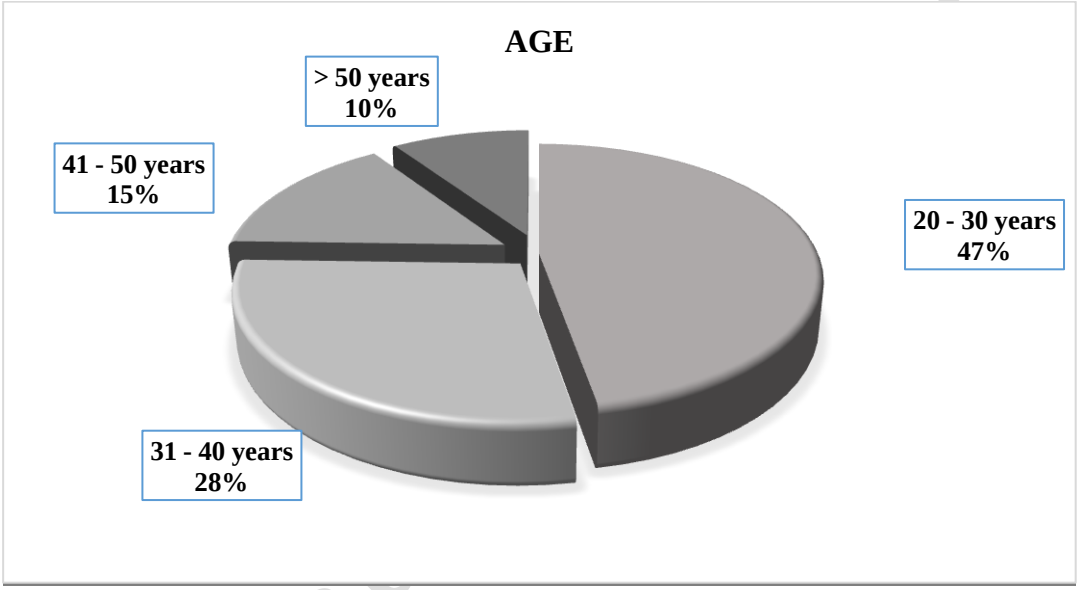



**Figure 4.4: Age of Respondents**

**Source: Survey Data (2018)**

### 4.3.3 Level of Education

According to Roy and Hord, 2004, lack of highly qualified and experienced staff is a barrier to organizational performance. In this regard, the study sought to establish the level of education of the respondents. The analysis results are as presented in figure 4.5:

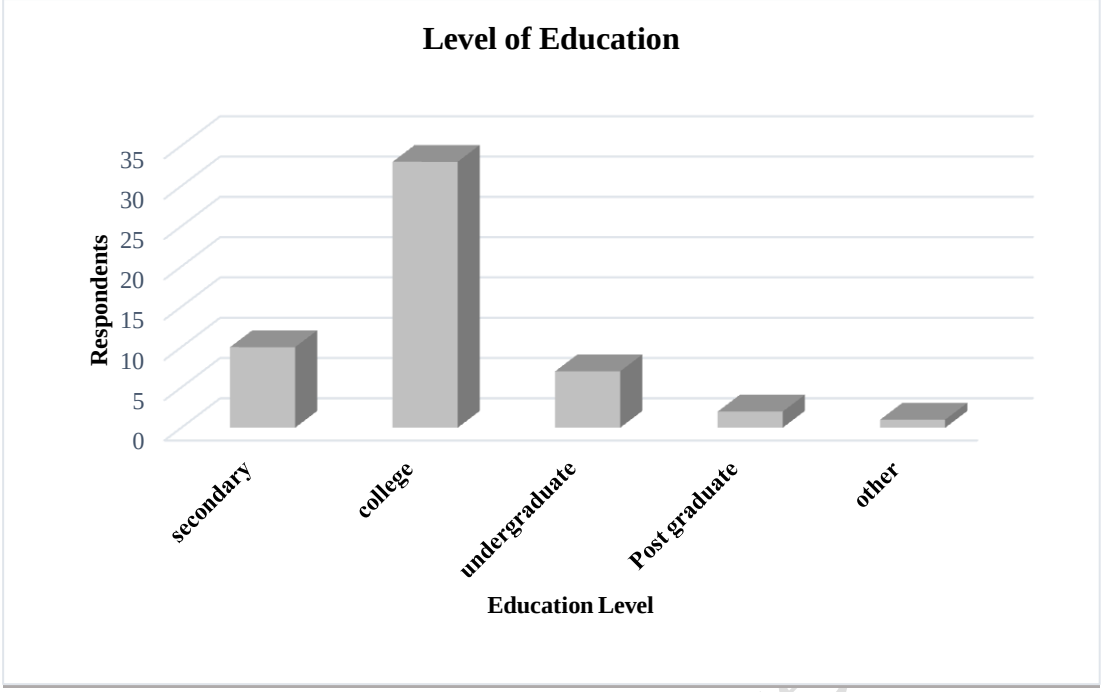



**Figure 4.5: Level of Education**

**Source: Survey Data (2018)**

It was established that 10(18.9%) of the respondents possessed secondary education, 33(62.3%) had college education .Further, 7(13.2%) had undergraduate level and 2 (3.8%) were post graduates. Only one respondent failed to disclose. The analysis of education level showed that majority of the respondents had college education. This was a good indication that the company had qualified employees who are knowledgeable and thus could answer the research questions with ease.

### 4.3.4 Years of Service

Work experience is key to performance of an organization. The study sought to establish the years of service that the respondents had served in the company. The analysis of the results were as presented in figure 4.6

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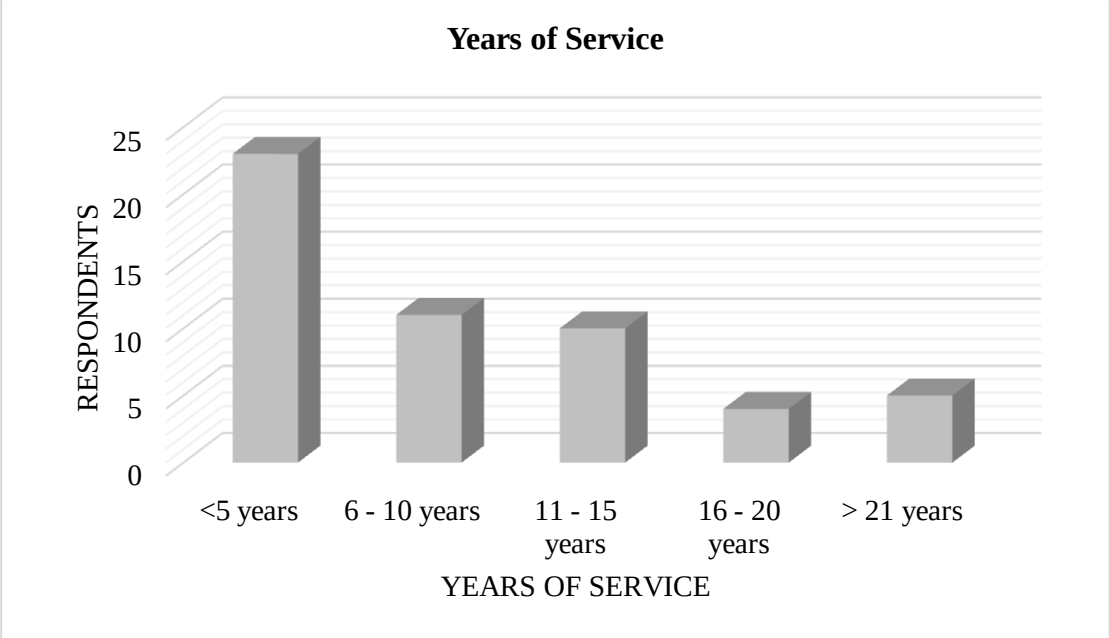



**Figure 4.6: Years of Service**

**Source: Survey Data (2018)**

Figure 4.6 indicates that majority of the respondents had served for a period of less than five years at 43.4%. 16.9% served for over 15 years. The rest of the respondents at 20.8% and 18.9% indicated to have served for a period of at most 6years and 15years respectively. Thus, the respondents who participated in the study had served the company for a considerable period of time hence were in a position to give credible information relating to the study.

### 4.3.5 Level of Employment

The study sought to establish the level of employment that the respondents belonged to in the organization. The analysis of the results was presented in figure 4.7.

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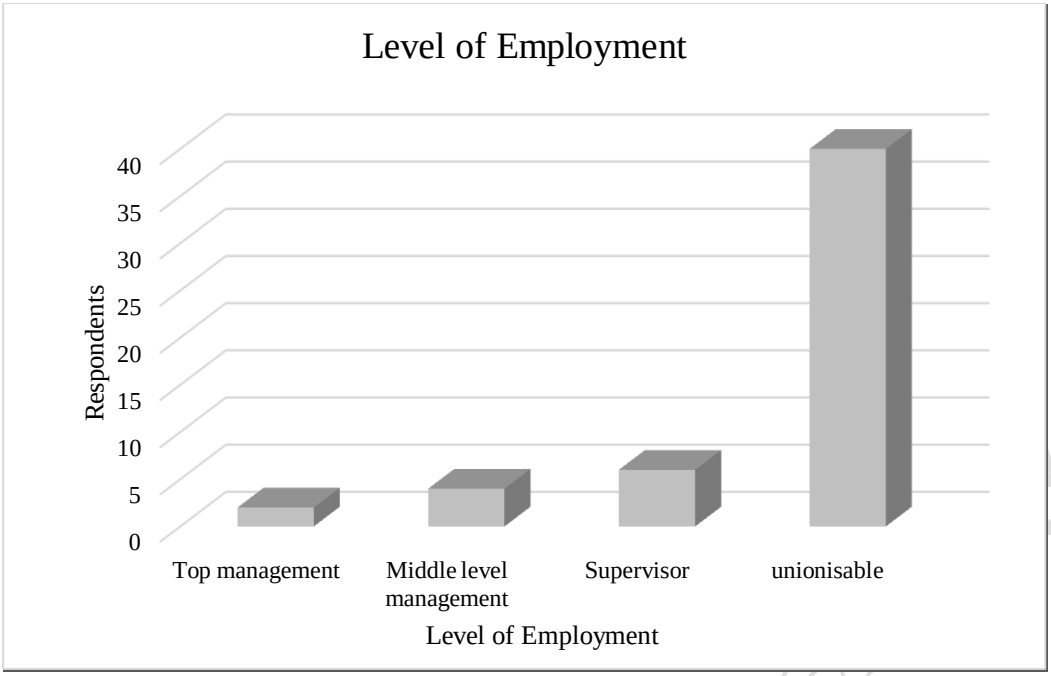



**Figure 4.7: Level of Employment**

**Source: Survey Data (2018)**

The findings revealed that 2(3.8%) of the respondents were in the top management, 4(7.5%) were in middle level management, 6 (11.3%) at the supervisory level whereas 40(75.5%) were unionisable staff. The analysis confirms that the target functional areas were fairly represented in the study therefore giving a complete representation of the organization echelons.

## 4.4 Descriptive Statistics

### 4.4.1 Board Structure

The board structure was measured using various indicators. This included the number of board members, number of board meetings, board diversity in terms of age, gender and experience, existence of a board calendar, length of board meetings and board skills. All the indicators were analyzed descriptively as indicated table 4.3:

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**Table 4.3: Descriptive Statistics for Board Structure**

| **Board Structure** | N | Minimum | Maximum | Mean | Std. Dev. |
|---|---|---|---|---|---|
| Number of board members is sufficient to oversee MACHWASCO | 53 | 1 | 5 | 3.85 | .886 |
| The number of board meetings is sufficient to deliberate on emerging issues | 53 | 1 | 5 | 3.89 | .974 |
| The board diversity is enough in terms of age, gender, experience and expertise | 53 | 1 | 5 | 3.98 | 1.047 |
| The board has a calendar and updates events affecting board meetings | 52 | 1 | 5 | 3.87 | .950 |
| The board allocates sufficient time for discussion before making decisions | 53 | 1 | 5 | 3.85 | 1.133 |
| The board members have relevant expertise to run the company | 53 | 1 | 5 | 4.13 | .900 |
| **Aggregate Score on Board Structure** | 52 | | | 3.928 | 0.981 |

**Source: Survey Data (2018)**

Table 4.3 indicates that, there is an aggregate mean score on board structure of 3.93 which is approximated at 4.0 of the 5 point likert scale adopted for use in this study. The table also shows that there is a minimal variability from the mean response since the study has an aggregate standard deviation score of 0.981. The aggregate score indicates that there is a unanimous agreement by the respondents on issues concerning the board of the company. This is further powered by the majority of a mean of 4.13 and standard deviation of 0.9 that the board members have the relevant expertise to run the company. However, a huge variability on the time the board allocates on discussions before making decisions with a mean of 3.85 and a standard deviation of 1.133 is indicated.

### 4.4.2 Strategic Roles of the Board

To determine the strategic roles of the board on the performance of MACHWASCO, various aspects were considered limited to the company's strategic plan, monitoring and evaluation on the implementation of the strategic plan, adoption of performance

management, and continuous monitoring, review and control. In addition, it also evaluated existence of quality objectives and monitoring and review of their attainment. This is as presented in the table 4.4:

**Table 4.4: Descriptive Statistics for Strategic Roles of the Board**

| **Strategic Roles of the Board** | N | Minimum | Maximum | Mean | Std. Dev. |
|---|---|---|---|---|---|
| The company strategic plan plays a vital role on its performance | 53 | 1 | 5 | 3.72 | .948 |
| The board continuously monitors and evaluates the implementation of the strategic plan | 53 | 1 | 5 | 3.87 | 1.075 |
| The company has adopted the use of performance Contracts to manage performance are se on target | 53 | 1 | 5 | 3.91 | 1.114 |
| The board has mechanisms in place for continuous monitoring reviewing and control performance | 50 | 1 | 5 | 3.92 | 1.047 |
| The company has quality objectives which guide performance monitoring and review | 50 | 1 | 5 | 3.90 | .974 |
| The board meets regularly to monitor, review and communicate feedback on performance | 53 | 1 | 5 | 4.15 | 1.026 |
| **Aggregate Score on Strategic Roles of the Board** | | | | 3.91 | 1.03 |

**Source: Survey Data (2018)**

Table 4.4 indicates that there is a mean aggregate score on the strategic roles of the board of 3.91 which is approximated at 4.0 on the 5 point likert scale used for this study. It indicates that, the respondents agrees with the strategic roles of the board. There is however a huge variability on the responses with an aggregate standard deviation of 1.03 indicating that not all respondents were of the same view. Among the issues interrogated, there was only a minimal variability on the role of the

strategic plan and existence of quality objectives only with standard deviation of 0.948 and 0.974 respectively.

### 4.4.3 Corporate Leadership

Corporate leadership involves all the tenets of leading and managing a corporation. It envisages many elements since leadership is diverse and evolves on daily basis. For the purpose of this study on corporate governance, the main issues interrogated included separation of roles of the CEO and the Chairman, organizational environment to promote performance, employee motivation, and role of Chairman Leadership and leadership styles employed on the company of study. The results obtained are presented in table 4.5:

**Table 4.5: Descriptive Statistics for Corporate Leadership**

| **Corporate Leadership** | N | Minimum | Maximum | Mean | Std. Dev. |
|---|---|---|---|---|---|
| There is clear separation of the roles of the MD and those of the Chairperson of the board | 53 | 1 | 5 | 3.96 | .898 |
| The management provides enabling environment for achievement of organizational goals | 53 | 1 | 5 | 3.77 | .974 |
| The board provides and sustains the necessary motivation within the company's workforce | 51 | 2 | 5 | 4.04 | .824 |
| The separation of chairman and CEO roles creates environment which improves the company's performance | 53 | 2 | 5 | 4.19 | .761 |
| The chairman leadership plays an important role in driving the agenda of the company forward | 53 | 1 | 5 | 3.91 | .925 |
| The leadership styles employed in the company enhances accountability and participation | 53 | 1 | 5 | 3.98 | .951 |
| **Aggregate Score on Corporate Leadership** | | | | 3.98 | 0.889 |

**Source: Survey Data (2018)**

This study sought to establish the influence of corporate leadership on the performance of water companies in Kenya. It revealed with an aggregate mean score of 3.98 which was approximated at 4.0 on the 5 point likert scale used. This was an indication that the respondents agreed on the issues interrogated on corporate performance. Further, there was a minimal variability of 0.889 standard deviation indicating that there was a unilateral agreement among majority of the respondents on the influence of corporate leadership on performance.

### 4.4.4 Board Independence

The independence of the board in managing the company was studied. Some of the aspects interrogated in the study included board member recruitment, existence of non-executive members tenure of board members, internal audit function, audit committees, communication and feedback between the audit committee and internal auditors and board independence in decision making. The descriptive statistics for board independence is as presented in table 4.6:

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**Table 4.6: Descriptive Statistics for Board Independence**

| **Board Independence** | N | Minimum | Maximum | Mean | Std. Deviation |
|---|---|---|---|---|---|
| Board members are recruited by an independent board nomination committee | 53 | 1 | 5 | 3.55 | .932 |
| The company has two thirds of board members as independent non-executive | 53 | 1 | 5 | 3.96 | .808 |
| The age and duration of service of a board member affects the performance of the company | 50 | 1 | 5 | 3.70 | 1.165 |
| There is well established independent and resourceful internal audit function | 53 | 1 | 5 | 4.04 | .919 |
| The audit committee plays a key role in monitoring controlling transparency and accountability | 52 | 1 | 5 | 4.04 | .928 |
| There is constant communication and feedback between the internal audit function and audit committee | 53 | 1 | 5 | 4.02 | .888 |
| **Aggregate Score on Board Independence** | | | | 3.98 | 0.94 |

**Source: Survey data (2018)**

Table 4.6 indicates that there was a mean aggregate score of 3.98 which is approximated to 4.0 on the 5 point likert scale adopted for use in the study. This indicated that the respondents agreed on the board independence. Further, a standard deviation of 0.94 indicated that there was a low variability. This meant that that the respondents shared almost the same view regarding the board independence. The respondents however a varied opinion on the recruitment of board members with the lowest mean in the cluster of 3.55 and a standard deviation of 0.92 indicating that there was unanimous agreement on the issues. This casted light on the respondents doubts on the recruitment process of the independent board. Further on the duration of service of board members with a mean of 3.70, there was a high variability indicating the respondents mixed views on the tenure of the board members which could be too long or too short.

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### 4.4.5 Performance of Machakos Water and Sewerage Company

Performance was measured using various indicators. These indicators included improved customer satisfaction, growth in area of coverage, reduction of non-revenue water, increase in revenue growth, improved service delivery and increase in efficiency and effectiveness of the company. The analysis is as presented in table 4.7:

**Table 4.7: Descriptive Statistics for Performance**

| **Performance** | N | Minimum | Maximum | Mean | Std. Dev. |
|---|---|---|---|---|---|
| Corporate governance has led to improvement in customer satisfaction | 53 | 1 | 5 | 3.79 | .793 |
| Through proper governance the company has recorded growth in its area of coverage | 52 | 1 | 5 | 4.04 | .766 |
| Close monitoring and controls has led to reduction of non-revenue water | 53 | 1 | 5 | 3.94 | .818 |
| Corporate governance has led to increase in revenue growth over the last five years | 52 | | 5 | 4.12 | .832 |
| Over the last five years the Company has improved in terms of service delivery | 52 | 1 | 5 | 4.00 | .816 |
| Proper corporate governance has resulted in efficiency and effectiveness in performance of the company | 53 | 1 | 5 | 4.08 | .895 |
| Aggregate Score on Performance | | | | 4.00 | 0.82 |

**Source: Survey Data (2018)**

Table 4.7 shows that the aggregate mean score was 4.00 which is equal to 4.00 (agree) on the 5 point likert scale used and a standard deviation of al indicators of performance as 0.82. This confirmed that the respondents were in agreement that the indicators determined were available in the MACHWASCO hence performance. There was a low aggregate standard deviation of 0.82 revealing narrow variability meaning that the aggregate mean response was stable and reliable hence a meaningful estimator of the population mean confirming performance in water companies. The respondents gave the least rating on corporate governance lead to improved customer

satisfaction with a mean of 3.79 and standard deviation of 0.79 indicating a very narrow variability on the mean.

### 4. 5 Test of Assumptions of Regression Analysis

The researcher used regression analysis to answer the research questions and draw an inference and conclusions on corporate governance and performance. To determine the appropriateness of the data, diagnostics test were carried out. According to Chatterjee and Hadi (2012) testing of assumptions is an important requirement for researcher's using multiple regression analysis since violation of multiple regression analysis can result to biased estimation of relationships, wrong coefficient estimates and untrusted coefficient levels. The researcher used sampling adequacy.

#### 4.5.1 Test of Sampling Adequacy

The sampling adequacy test is also called the Kaiser-Meyer-Olkin measure (KMO) and the Bartlett's Test of Sphericity was performed to establish sampling adequacy of the research data. The KMO measures varies between 0 and 1 and values closer to 1 are better with a threshold of 0.5. Brown and Onsman (2012) stated that KMO of 0.50 is acceptable degree for sampling adequacy. The study revealed a KMO of 0.621 as presented in table below.

**Table 4.8: KMO and Bartlett's Test**

| **KMO and Bartlett's Test** | | |
|---|---|---|
| Kaiser-Meyer-Olkin Measure of Sampling Adequacy. | | .621 |
| Bartlett's Test of Sphericity | Approx. Chi-Square | 861.377 |
| | Df | 300 |
| | Sig. | .000 |

**Source: Data Survey (2018)**

As per Brown and Onesman (2012) criterion that a KMO of range 0.524 and 0.733 is acceptable with the study yielding a KMO of 0.621 while Bartlett's test of sphericity had a consistent significance of calculated probability of 0.000 well below the 0.05 threshold. Therefore, the research sample was adequate, factorable and further statistical analysis could be performed.

### 4.6 Inferential Statistics

Multivariate analysis was carried out to investigate the influence of corporate governance on performance of Machakos Water and Sewerage Company. In this respect, board structure, board strategy, corporate leadership board independence were jointly regressed on performance. The results of the multiple regression analysis are presented in Tables 4.9, 4.10 and 4.11

**Table 4.9: Analysis of Variance**

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|---|---|---|---|---|---|
| Regression | 194.544 | 4 | 48.636 | 7.804 | .000[b] |
| Residual | 299.136 | 48 | 6.232 | | |
| Total | 493.680 | 52 | | | |

a. Dependent Variable: Performance

b. Predictors: (Constant), Board Independence, Corporate Leadership, Board Structure, Strategic roles of the Board

**Source: Survey Data (2018)**

To determine the goodness of fit of the regression model, an analysis of variance (ANOVA) was conducted which yielded a significance level of 0.00% indicating that the model had goodness of fit to establish the relationship between the independent and dependent variables since the model had a significance level (P-level) of less than 5%. The significance level indicated F critical value (from F tables) of 2.45 while the value of F calculated was 7.804. Since the calculated F value is greater than the F critical value, this was a good indication that the overall regression model was sufficient and significant in predicting the relation between corporate governance and performance.

**Table 4.10: Model Summary**

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|---|---|---|---|---|
| 1 | .628[a] | .394 | .344 | 2.496 |

**Source: Survey Data (2018)**

From table 4.10, R in the above table denotes the correlation coefficient which shows the relationship between variables of study. The study resulted to R value of 0.628 which indicated a strong correlation between the variables of study both independent and dependent. The value R squared was 0.394 with adjusted R squared value of 0.344 implying that the four dimensions of corporate governance are responsible for 34.4% of variations in performance of the water company as other factors affect performance by 65.6%.

**Table 4.11: Regression Results for Direct Relationship**

| Model | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|---|---|---|---|---|---|
| | B | Std. Error | Beta | | |
| (Constant) | 12.686 | 3.324 | | 3.816 | .000 |
| Board Structure | .333 | .202 | .277 | 1.645 | .016 |
| Strategic Roles of the Board | .633 | .134 | .827 | 4.720 | .000 |
| Corporate Leadership | .267 | .146 | .338 | 1.823 | .057 |
| Board Independence | .226 | .136 | .271 | 1.658 | .014 |

**Source: Data Survey (2018**

The regression model estimated through the results of regression analysis in table 4.11 is presented below:

**Performance = 12.69+ 0.33 Board structure + 0.633 strategic roles of the board +0.267 Corporate Leadership + 0.226 Board Independence**

The model indicated that if all variables of the study are held constant then performance of the water company would be at 12.69 units. A unit increase in board structure would lead to 0.333 change in the Company's performance. A unit increase

in strategic roles of the board would result into 0.633 change in performance, as a corporate leadership and board independence a unit change would result to 0.267 and 0.226 increase in performance respectively.

A t statistics test was also carried out to determine the relative importance of each variable in the model. The study guide adopted regarding assessing the usefulness of the predictors assumed t values of below -0.5 or above 0.5. In respect to this the most important variable was strategic roles of the board, board structure, corporate leadership and board independence.

### 4.6.1 Specific Objective One

The first objective of the study was to establish the influence of board structure on performance of water companies in Kenya. A regression model in Table 4.11 indicated that board structure is statistically significant with $\beta$=0.333; t=1.64 and p=0.016. This meant that at 95% confidence level, board structure has a positive effect on performance. The results confirms that board structure is responsible for 0.33 increase in performance. It was therefore concluded that there is a relationship between board structure and performance which was in line with Opanga (2013) who sought to establish the effect of board structure in reference to the number of board committees, board meetings frequency and number of board of directors and found a positive correlation with financial performance.

This conforms with Canella, and Paetzold (2000) who asserts that RBT focuses on the role played by the board in providing essential resources to an organization through their linkages to the external environment. It provides a focus on the involvement of independent representatives in the organization who act as a link between the organization and the environment and as a means of accessing resources that are critical.

### 4.6.2 Specific Objective Two

The second specific objective was to shade light on the impact of the strategic roles of the board on performance of water service providers in Kenya. The regression results in table 4.11showed that strategic roles of the board were statistically significant with a $\beta$ = 0.633, t= 4.72 and p=0.000. At 95% level of confidence, strategic roles of the

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board has a positive effect on performance of the WSP. Thus, the results demonstrates that a unit increase in strategic roles of the board is responsible for 0.633 increase in performance.

The findings are in support of Hyvari (2016) who investigated on the roles of top management in the effective company strategy implementation. The findings of the study revealed that the board distributes rights and responsibilities among different participants in the organization, and is responsible for monitoring, control and directing which impacts on the performance. Ng'etich (2015) studied on corporate governance and financial performance of water companies in Kenya. In his findings, the study revealed that there is a positive relationship between financial performance and corporate governance.

### 4.6.3 Specific Objective Three

The third specific objective of the study was to analyze the influence of corporate leadership on performance. The regression results in table 4.11 revealed that corporate leadership was statistically significant with $\beta$=0.267, t = 1.823 and p =0.057. This was an indication that at 95% level of confidence, corporate leadership has a positive relationship with performance. In this case, a unit increase in corporate leadership accounts for 0.267 of the performance. Hence, the conclusion is that there is a relationship between corporate leadership and performance of Machakos Water and Sewerage Company.

The results corroborates with Wanjiku (2011) who undertook a study to assert how corporate governance practices relate to growth of companies listed in the Nairobi Securities Exchange. The study looked at issues like corporate communication, leadership, and technology application. The study revealed that there is a positive linear relation on corporate governance and growth in in those companies.

Stewardship theory helps give a deeper insight on inclined roles of independent directors and executives to operate the organization to maximize on performance as well as meet the interests of the shareholders of Machakos Water and Sewerage Company. Further it helped understand the corporate leadership and independence of

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the directors and hence extrapolate that managers are contracted with a prime motive of generating wealth to the shareholders and there is consequences for performance.

### 4.6.4 Specific Objective Four

The fourth specific objective was to determine the influence of board independence on the performance of WSPs. The study revealed as tabulated on table 4. 11 that $\beta$ = 0.226, t = 1.83 and p = 0.014. This was an indication the at 95% confidence level, board independence has positive relationship with performance. This reveals that a unit increase in board independence results in 0.226 increase in performance. The researcher therefore concludes that there is a relationship between board independence and performance of Machakos Water and Sewerage Company.

These results supported Ahmed and Hamdan (2015) who established that the board of directors were controlled by a large number of independent directors. Further, they established that the position of the CEO and chairman were split as the chairman was an independent director. This is in line with good corporate leadership structure as the chairman has a great power for independent decision making of the board. However, the study used secondary data and therefore the findings could not be generalised.

Under agency theory, Green (2008), argued that ownership and control in a large organization is often seen as a way of creating power base for executive, which is the management. This is so because the critical information is available to managers who are delegated to run the organization and this can make them act in a manner which will give them undue gain at the expense of stakeholder's interests. It is therefore the mandate of the board to oversee, monitor and evaluate the activities of the executive objectively for malpractices. It is also grounded on the fact that people have self-interests instead of being self-sacrificing hence cannot be trusted to act in the best interest of others as they seek to maximize their own utility (Opanga, 2013).

## 4.7 Analysis of Qualitative Data

The researcher sought to get a personalized opinions on some issues affecting the study. The study sought to qualitatively determine the respondent's views on the benefits the company derives from having a board of directors. Majority were of the

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opinion that the board directs duties to the Managing Director, oversees the sooth running of the company, and ensures supervision and governance. This was a clear indication that there is a good understanding on the benefits of the company to have a board in place.

Further, the researcher wanted to establish how else corporate governance shaped the performance of MACHWASCO. The respondents cited employee motivation, creation or enabling environment to boost performance, ensured competitive recruitment process. The board ensured effective policies and strategic objectives of the company were specific, measurable, attainable, realistic and timely. This was an indication that the role of the board of directors in MACHWASCO was holistic in nature towards improving the performance of the company taking into consideration both employees needs and company needs.

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# CHAPTER FIVE

# SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

## 5.1 Introduction

This chapter gives a brief summary of the findings, conclusions, and recommendations. The prime motive of the study was to establish the relationship between corporate governance and performance of water service providers in Kenya. The specific objectives were to determine the influence of board structure, strategic roles of the board, corporate leadership and board independence on performance of water service providers in Kenya.

## 5.2 Summary

The first specific objective was to determine the influence of board structure on the performance water service providers. The study revealed that elements and activities relating to of board structure where practiced this included, optimal number of board members, sufficient board meetings, board diversity, board calendar, board sitting and expertise. The study revealed that though board structure is very critical, elements related to it had different levels of emphasis in WSPs. The study had a prior expectation that board structure has relationship with the overall performance of the company an assertion which was confirmed through statistical analysis that board structure positively influence organizational; performance

The second specific objective was to establish the relationship between strategic roles of the board and performance. Ideally, all the strategic roles of the board were found to be practiced but in varying extends. The statistical inferences computed indicated that strategic roles of the board had a positive contribution to performance with the highest noticeable effect in terms of coefficients. The activities and elements determined include strategic plan, monitoring and evaluation of implementation of strategic plan, performance contracting, performance management, existence of quality objectives and communication.

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The third objective was to determine the relationship and influence of corporate leadership on the performance of WSPs. The areas considered were limited to separation of roles between the CEO and the board chairperson, business environment, motivation of employees, chairman's leadership and leadership styles. Inferential statistics drawn indicated that there was a relationship between corporate leadership and performance however, it was evident that it had the least effect on performance. This was in line with the researchers expectations that corporate leadership has a positive relation with performance.

The fourth specific object was to establish the influence of board independence on performance. The study revealed that there was a positive statistical relationship between board independence and organizational performance. The issues of concern were limited to appointment of board members, board composition, period of tenure, monitoring and evaluation, audit committee and independent decision making.

### 5.3 Contributions of the study to Knowledge

The study was to investigate the effect of corporate governance on the performance of water service providers in Kenya. The empirical studies established that corporate governance has a significant effect on performance. However, it is notable that most of the studies conducted were on the Banking industry. Further, those studies which focused on water service provision were focused on different objectives. Some of the studies had limitations relating to methodology, context, consistency of results and conceptualization.

The study was conducted in local context with the empirical review conducted on similar studies indicating that corporate governance influence performance. It considered diverse issues like board structure, instead of board composition, corporate leadership and strategic roles of the board making it unique therefore adding to the body of knowledge on corporate governance.

The study added to the body of knowledge fundamental to both practitioners and researchers in water service sector. It is crucial as it addressed keys issues with the policy framework of the Government. Under Vision 2030, the six sustainable

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development goal (SDGs) ensures availability and sustainable management of water and sanitation for all Gok (2015). Therefore the study is critical as it addresses corporate governance issues which have direct effect on the realization of the SDG.

### 5.4 Conclusion

Performance is the key concern of the management of all organizations. It is a diverse element with many indicators thereby presenting challenge in its determination. For the purpose of this study, it was measure using customer satisfaction, growth in revenue, reduction in none revenue water, growth in coverage are, improved efficiency and service delivery. The study investigated the relationship between corporate governance and performance in WSPs.

The inferential computed generated very critical conclusions. It established that board structure is statistically significant therefore there is a significant relationship between board structure and performance. Similar, the study inferred that strategic roles of the board has the greatest effect on performance showing that the two have a very strong relationship. The third and fourth objective was to establish the relationship between corporate leadership and board independent on leadership. The study revealed that both had a minimal effect on the overall performance of the WSP.

### 5.4 Recommendations

In order to achieve optimal performance, it is critical to ensure that all the four areas are well mixed to bring out maximum synergy. Maximizing on strategic roles of the board will have the greatest and immediate effect on the overall performance of the company. Therefore, the company needs to capitalize on the elements of board structure to trap its maximum effect.

The WSPs are in service provision industry were customer satisfaction is key for attainment of other performance indicators like growth in revenue and coverage. Companies therefore need to be more sensitive on customer focused issues in relation to governance. From the study, corporate governance has significant effect on performance therefore corporates needs to adopt and practice good corporate governance practices.

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To ensure there is accountability and board independency, selection of board members need to be through a competitive recruitment process rather than reservations of certain representations due to organizational stakes and superiority.

### 5.5 Suggestion for Further Study

The study was conducted on the influence of corporate governance on performance of water service providers focussing on non-financial measures. Studies should be carried out to establish the effect corporate governance with a focus on non-financial indicators in other sectors. The researcher further suggests studies on corporate governance and its effects on non-financial performance indicators like employee motivation, employee satisfaction and organizational reputation within and without service provision industry.

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## Appendix i: Letter of Introduction

Winfred Mbai,

St. Paul's University,

28/02/2018

**To: Respondents**

Dear respondent,

**RE: INTRODUCTION LETTER**

I am a student at St Paul's University currently pursuing a Master degree in Business Administration specializing in strategic management. To successfully complete the studies, it is a requirement by the institution that a student conducts a research project in a related field of study.

To accomplish this purpose, I am currently carrying out a study on '**Influence of corporate governance on performance water service providers in Kenya: case of Machakos Water and Sewerage Company'**. I therefore take this opportunity to introduce my questionnaire and request that you provide me the required information. Kindly note that all the information provided therein will be treated with uttermost confidentiality and will only be used for the purpose of the research study only.

Thank you for taking your time to fill the questionnaire and your cooperation.

Yours sincerely,

**Winfred Mbai**

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## Appendix ii: Questionnaire

**Instructions**

*You are kindly invited to fill-in the questionnaire. This questionnaire will help in data collection to facilitate deeper insight on Corporate Governance and performance of water service providers: A case of Machakos Water and Sewerage Company. The questionnaire has two sections. Please complete as per instructions. Do not indicate your name or any form of identification on the questionnaire.*

### SECTION A: Background Information

*Please tick (√) where appropriate*

1) Please indicate your gender

   ` Male [ ] Female [ ]

2) Kindly indicate your age bracket

   Below 19 years [ ]
   20-30 years [ ]
   31-40years [ ]
   41-50years [ ]
   51 years and above [ ]

3) What is your level of education?

   Secondary [ ]
   College [ ]
   Undergraduate [ ]
   Postgraduate [ ]
   Any other (please specify) [ ]

4) For how long have your served in the company?

   0-5 years [ ]
   6-10 years [ ]
   11-15 years [ ]
   16-20 years [ ]
   Above 21 years [ ]

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5) What is your level of employment?

Top-level Manager [ ]
Middle-level Manager [ ]
Supervisor [ ]
Unionisable Staff [ ]

## Section B: General Information

On a scale of 1-5, please indicate your level of agreement with the following statements (where; 1- Strongly disagree, 2- Disagree, 3- Moderately agree 4- Agree, 5- strongly agree)

**6) Board Structure**

| Statement | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|
| The number of board members is sufficient to oversee running of the company. | | | | | |
| The board meetings are sufficient to deliberate on emerging and existing issues. | | | | | |
| The board is diverse enough in terms of age, gender, experience and expertise. | | | | | |
| Board members have a calendar and updates events affecting board meetings. | | | | | |
| The board allocates sufficient time for discussion before making decisions. | | | | | |
| The board members have the relevant expertise to run the company | | | | | |

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**7) Strategic Roles of the Board**

| Statement | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|
| The company has strategic plan plays a vital role on its performance | | | | | |
| The board continuously monitors and evaluates the implementation of the strategic plan | | | | | |
| The company has adopted the use of performance contracts to manage performance on set targets | | | | | |
| The board has mechanisms in place for continuous monitoring, review and control performance | | | | | |
| The company has quality objectives which guide performance monitoring and review | | | | | |
| The board meets regularly to monitor, review and communicate feedback on performance | | | | | |

**8) Corporate Leadership**

| Statement | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|
| There is clear separation of the roles of the Managing Director and those of Chairperson of the board | | | | | |
| The management provides enabling environment for achievement of organizational goals. | | | | | |
| The board provides and sustains the necessary motivation within the company's workforce. | | | | | |

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| | | | | | |
|---|---|---|---|---|---|
| The separation of chairman and CEO roles creates environment which improves company performance | | | | | |
| The chairman leadership plays an important role in driving the agenda of the company forward | | | | | |
| The leadership styles employed in the company enhances accountability and participation | | | | | |

**9) Board Independence**

| Statement | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|
| Board members are recruited by an independent board nomination committee | | | | | |
| The company has two-thirds of board members as independent non-executive directors | | | | | |
| The age and duration of service of a board member affects the performance of the company. | | | | | |
| There is well established, independent and resourceful internal audit function. | | | | | |
| The audit committee plays a key role in monitoring, controlling, transparency and accountability | | | | | |
| There is a constant communication and feedback between the internal audit function and audit committee | | | | | |
| The board is independent in decision making as it is not influenced by external or internal forces | | | | | |

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**10) Performance**

Kindly indicate the level at which you agree with the following statements on corporate governance impact on performance of performance of MACHWASCO (1- Strongly disagree, 2- Disagree, 3- Moderately agree, 4- Agree, 5- Strongly agree)

| Statement | 1 | 2 | 3 | 4 | 5 |
|---|---|---|---|---|---|
| Corporate governance has led to improvement in customer satisfaction. | | | | | |
| Through proper governance the company has recorded growth in its area of coverage | | | | | |
| Close monitoring and controls has led to reduction of non-revenue water | | | | | |
| Corporate governance has led to increase in revenue growth over the last five years | | | | | |
| Over the last five years, the company has improved in terms of service delivery | | | | | |
| Proper corporate governance has resulted in efficiency and effectiveness in performance of the company | | | | | |

11) In brief, kindly quote some of the benefits the company derives from having its board of directors in place

_____

_____

_____

_____

_____

_____

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12) How else has corporate governance shaped performance of MACHWASCO?

_____

_____

_____

_____

_____

_____

_____

_____

**Thank you**

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## Appendix iii: Recommendation Letter

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**Appendix iv: NACOSTI Research Permit**

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