

Influence of Governance Factors on Performance of Firms Listed at Nairobi Securities Exchange, Kenya

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Abstract

This study examined how governance factors influence the performance of firms listed on the Nairobi Securities Exchange. Adopting a positivist philosophy, it used both descriptive and explanatory research designs. The analysis focused on 61 listed firms, with heads of finance, marketing, HR, internal audit, customer relations, operations, ICT, and risk and compliance as the units of observation. The target population comprised 350 departmental heads, from which a sample of 187 respondents was selected using purposive and stratified random sampling, achieving a 97% response rate. Data collection involved semi-structured questionnaires for primary data and extraction checklists for secondary data. Qualitative data was analyzed thematically, while quantitative data was analyzed using descriptive statistics such as frequencies and percentages, and inferential statistics, including logistic regression. The Nagelkerke Pseudo R^2 indicated that governance factors explained 60.2% of the variance in firm performance ($R^2 = .602$), and the regression coefficient showed that governance factors significantly predicted performance ($B = 3.072, p \leq .05$). The study concludes that firm performance—measured by financial outcomes, customer satisfaction, internal processes, and learning and growth—can be enhanced through the adoption of governance (ESG) practices. This study recommends that management of NSE-listed firms integrate governance practices into their core operations to improve overall performance.

Key Words: Firms Listed at Nairobi Securities Exchange, Governance Factors, Organizational Performance

Introduction

Sustainability factors are key organizational aspects measured by long-term societal and environmental contributions, ethical conduct, and responsible corporate governance (Abbasi & Alvarado, 2022). They include how firms address environmental issues, social responsibility, and governance (Clementino & Perkins, 2021). Investors and stakeholders increasingly value these criteria for assessing a company's viability and risk management (Xu & Zhu, 2024). Sustainability factors also attract investment, as socially responsible investors prefer organizations aligned with their values (Popescu et al., 2022). Ahmad et al. (2024) note that sustainability factors cover practices and strategies for responsible, ethical, and impactful operations. Alagbe (2021) and Arvidsson and Dumay (2022) define sustainability factors as

environmental, social, and governance (ESG) considerations. This research focused on governance factors.

Governance factors include leadership structure, internal control, risk management, shareholder rights, executive compensation, and ethical conduct, ensuring transparency and accountability (Annesi et al., 2024). They are essential for firm performance, providing a framework for transparency and ethical conduct at all levels (Mooneepen & Mamode Khan, 2022). In China, strong governance practices, such as diverse boards and clear compensation policies, enhance decision-making (Chen et al., 2023).

Consistent governance processes aligned with strategic objectives and stakeholder expectations positively shape firm performance. In Nigeria, promoting honesty and regulatory adherence reduces risks and boosts reputation, with governance disclosures accounting for 18.9% of performance (Funmilayo, 2022). In Uganda, transparent governance improves efficiency and financial stability, while informed decision-making sustains growth (Awuor, 2023). Effective governance systems also attract and retain talent, contributing 17.9% of firm value for NSE-listed companies (Mumo, 2022).

Moreover, NSE-listed firms have also experienced losses in their share and customer satisfaction (Machiri et al., 2024). Although it is evident that more than three-quarters of the firms show levels of sustainability reporting, only a quarter of them is abiding by the NSE sustainability policy fully (Mwendwa, 2023). The mismatch between the number of companies that report on ESG and the one that complies with the guidelines provided by NSE identifies a gap in the policy. Some of the challenges in this regard are the high carbon emissions, poor waste management, occasional stakeholder involvement, and bad governance (Onwere, 2024). These issues imply that there is a managerial gap in the proper implementation of sustainability practices in the daily operations.

While leadership plays a critical role in driving sustainability initiatives, the performance issues faced by listed NSE firms may stem from a lack of clear strategic direction and inadequate systems for monitoring and measuring sustainability outcomes. To bridge this gap, it is recommended that companies focus on the practical application of sustainability strategies and implement robust monitoring systems to track and measure sustainability performance. This study will identify best practices and strategies for managers to enhance environmental, social and governance factors integration, address operational shortcomings, and ensure that sustainability is embedded within the organizational culture and decision-making processes.

Notably, while various studies have examined the relationship between governance factors and firm performance, they have approached the research from a narrow view. For instance, Agutu and Githira (2023) focused on financial performance, Serem et al. (2024) examine firm value, Maina (2021) looked at profitability, Masila et al. (2024) used financial performance, Mbuthia and Gatauwa (2022) and Ngangi and Ngali (2023) looked at financial performance measured in terms of return on equity and return on assets, Ngunjiri (2023) looked at financial performance measured in terms of return on assets and Mwaura et al. (2023) looked at performance in terms of sales turnover and market share. This study aims to address these gaps by framing organizational performance from a holistic perspective using the Balanced Scorecard (BSC).

Studies conducted on governance factors in Kenya show methodological, conceptual and contextual differences. Serem et al. (2024), Agutu and Githira (2023) and Mbuthia and Gatauwa (2022) used secondary data, while Maina (2021), Mwaura et al. (2023), Ngangi and Ngali (2023)

and Masila et al. (2024) relied on primary data from structured questionnaires. However, this study will make use of primary data, which will be collected by use of semi-structured questionnaires. Moreover, Agutu and Githira (2023) focused on financial firms, Mwaura et al. (2023) looked at family-led companies, Ngunjiri (2023) and Ngangi and Ngali (2023) focused on manufacturing firms, whilst Maina (2021) examined the Big Four professional services firms leaving a gap in understanding of how ESG impacts across all sectors and firm sizes listed at the NSE.

As a result, many executives are still uncertain about leveraging governance factors for business success. Further, despite the Nairobi Securities Exchange (NSE) launching its ESG Disclosures Guidance Manual in 2021, there are insufficient policy frameworks and regulatory incentives to ensure robust ESG adoption (Nairobi Securities Exchange, 2023). Muigua (2022) indicates that many NSE-listed firms have not fully integrated governance factors into their core strategies, viewing them as peripheral rather than core priorities. This gap leads to missed opportunities for leveraging governance for competitive advantage and sustainability.

Purpose of the Study

This study sought to examine the influence of governance factors on the performance of firms listed at Nairobi Securities Exchange. Through the identification of the influence of governance factors on firm performance, this study sought to bridge the existing knowledge gap and provide actionable insights for managers and policymakers.

Theoretical Review

This research study applied the Environmental, Social, and Governance (ESG) framework, focusing on the Governance pillar, as the guiding theory. The theory postulates that the performance of a firm is influenced not only by financial outcomes but also by the quality of its governance structures, including leadership, board composition, transparency, and ethical standards (Eccles & Klimenko, 2019; Meiden & Silaban, 2023). According to the ESG perspective, effective firms implement governance practices that ensure accountability, strategic alignment with shareholder interests, and risk mitigation in their operations and decision-making (Ferrell, 2021). Firms are therefore expected to adopt measures that strengthen ethical leadership, protect shareholder rights, and enhance transparency. The theory explains the influence of governance practices such as board effectiveness, executive accountability, and compliance with regulations on the performance of firms listed at the Nairobi Securities Exchange. Tang (2023) argues that in line with the ESG framework, firms with strong governance structures are better able to attract long-term investors, maintain stakeholder confidence, and reduce the likelihood of operational and reputational risks. By embedding robust governance practices into their strategic and operational processes, firms can improve decision-making, ensure regulatory compliance, and enhance their financial performance. The ESG governance pillar therefore provides a comprehensive explanation of how governance factors contribute to improved firm performance.

Conceptual Framework

Figure 1 shows the conceptual framework for this research study, and the relationship between the independent and dependent variables. The independent variable in this research study was the governance factors, and the dependent variable was performance of firms listed at Nairobi Securities Exchange, Kenya.

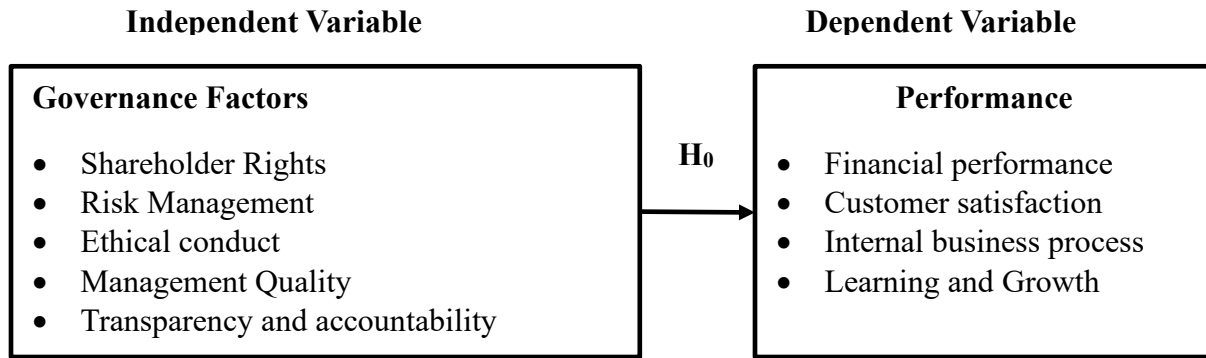


Figure 1

Conceptual framework

Empirical Review

Governance factors influence organizational performance by promoting accountability, ethical practices, and effective management. In Nigeria, Oke and Akinyemi (2021) examined the effect of board size, board independence, and audit committee effectiveness on financial performance of 50 listed companies over a ten-year period and found that independent boards and strong audit committees significantly enhanced return on equity (ROE) and return on assets (ROA). In Kenya, Abang’a, et al. (2022) investigated the effect of corporate governance on the capital budget realization of 45 state-owned enterprises from 2015 to 2018, reporting that board meetings, board skills, and gender diversity positively influenced performance. Omware et al. (2020) studied 11 commercial banks listed on the Nairobi Securities Exchange and found that board size, board independence, education, gender diversity, and ethnic composition positively affected financial performance. Similarly, Mukama and Kasozi (2023) examined firms in Uganda and reported that robust governance practices improved operational efficiency and financial outcomes.

Research Methodology

This research study employed the positivism research philosophy because it emphasizes empiricism and objectivity, which enables the testing of hypotheses as well as the analysis of associations between governance factors and the performance of firms listed at the Nairobi Securities Exchange. This research study also employed a combination of descriptive and explanatory research designs. The descriptive design is reliable in providing answers to questions of what, who, where, and how related to governance factors among firms, while the explanatory design enables the investigation of cause-effect relationships between governance factors and firm performance.

The target population was 350 heads of finance, marketing, human resources, internal audit, customer relations, operations, information and communication technology, and risk and compliance departments in 61 firms listed at the Nairobi Securities Exchange (NSE). This research study applied the multistage sampling method (purposive sampling and stratified random sampling) due to the various departments in the population. Yamane (1967) sample size formula was employed to determine the size of the sample, which resulted in a sample size of 187.

This study used both primary and secondary data. Secondary data came from annual reports and organizational documents of firms listed at the Nairobi Securities Exchange. Primary data was

collected via structured questionnaires administered to heads of key departments. Qualitative data was analyzed thematically using NVivo, while quantitative data was processed in SPSS (version 28) using descriptive statistics including percentages, mean, standard deviation and inferential methods, including logistic, multinomial, and stepwise regression. Logistic regression estimated the probability of firm performance based on governance factors

Results

This research study collected 181 of the 187 questionnaires administered, translating to a response rate of 96.8%. As part of the general information, the findings indicated that 38% of the participants in this study specified that they had served in their organizations for 11 to 20 years, while 34% indicated over 20 years. In addition, most of the departmental heads in firms listed at the Nairobi Securities Exchange (51%) had a master's degree and 33% had an undergraduate degree. The results depict that 67% of the organizations had more than 300 employees, 13% had fewer than 50 employees, and 7% had between 50 and 100 employees.

Descriptive Analysis

Shareholder rights, as a key governance indicator, entail transparency, equity in treatment, and regular communication of performance-related information to shareholders. From the results, respondents agreed that organizations ensure equal treatment of all shareholders, regardless of ownership stake ($M = 3.96$, $SD = 0.95$), and that shareholders are regularly informed about the organization's financial performance and strategic decisions ($M = 3.94$, $SD = 1.04$). These findings suggest that most firms uphold principles of fairness and disclosure in shareholder engagement. Risk management, which is a central component of governance, encompasses the presence of formal frameworks, proactive risk identification, and strategic responsiveness to emerging threats. From the results, respondents agreed that organizations proactively address emerging risks and adjust strategies accordingly ($M = 4.03$, $SD = 0.78$). They also indicated that firms have comprehensive risk management frameworks ($M = 3.94$, $SD = 0.97$) and regularly assess and mitigate operational risks ($M = 3.94$, $SD = 0.88$). These results suggest that most firms listed at the NSE maintain structured and responsive risk management systems.

Ethical conduct, as a key governance factor, entails the promotion of ethical values, the presence of formal ethical guidelines, and the integration of ethics into decision-making. Respondents agreed that organizations promote a strong culture of ethical conduct in all aspects of operations ($M = 3.83$, $SD = 1.03$) and maintain a code of ethics for employees and stakeholders ($M = 3.81$, $SD = 0.96$). Additionally, they indicated that ethical considerations are central to organizational decision-making processes ($M = 3.73$, $SD = 1.07$). These findings suggest that ethical governance is generally emphasized across listed firms.

Management quality, as a critical governance factor, involves leadership capability, investment in leadership development, and communication effectiveness. From the results, respondents agreed that leadership teams are skilled and capable of driving organizational success ($M = 3.80$, $SD = 1.01$), and that the organizations provide ongoing training and development for leaders ($M = 3.76$, $SD = 1.00$). Additionally, respondents strongly affirmed that leadership teams communicate effectively with employees and stakeholders ($M = 3.88$, $SD = 0.94$). These results suggest that most firms recognize the importance of strong and competent leadership.

Transparency and accountability, as essential governance factors, entail transparency in financial reporting, stakeholder accountability, and mechanisms for reporting and addressing organizational

misconduct. From the results, respondents agreed that organizations maintain high levels of transparency in financial reporting (M = 3.82, SD = 1.01). They also indicated that organization is committed to accountability to stakeholders for all decisions (M = 3.78, SD = 1.04), and that clear policies exist for reporting and addressing misconduct or failure to meet standards (M = 3.81, SD = 1.05). These findings suggest that listed firms place a considerable emphasis on integrity and accountability in their operations.

Correlation Analysis

The governance dimensions under consideration included indicators such as shareholder rights, risk management, ethical conduct, management quality, and transparency and accountability. As shown in Table 1, the analysis revealed a strong and statistically significant positive correlation between governance factors and firm performance, $r(179) = .738, p < .001$. This implies that there exists an association between governance factors and firm performance.

Table 1

Spearman's Rank Correlation for Governance Factors and Performance of Listed Firms

		Performance	Governance
		Factors	
Spearman's rho	Performance	Correlation Coefficient	1.000
		Sig. (2-tailed)	.738**
		N	.000
Governance Factors	Governance	Correlation Coefficient	181
		Sig. (2-tailed)	.738**
		N	181

** . Correlation is significant at the 0.01 level (2-tailed).

Regression Analysis of the Governance Factors on Performance of Listed Firms

To ensure the robustness, accuracy, and credibility of the regression analysis examining the influence of governance factors on firm performance, a series of diagnostic tests were undertaken. These tests included the Hosmer-Lemeshow test, Omnibus test, Cook's Distance, and the Wald test.

Hosmer-Lemeshow Test

The results of the Hosmer and Lemeshow test, with a Chi-square value of 4.151 and 7 degrees of freedom, yielded a p-value of 0.762. Since the p-value is greater than 0.05, this indicates that the model fits the data well. This confirms that the model is appropriate for the data and adequately represents the relationship between governance factors and firm performance.

Omnibus Test

The results show that the model has a Chi-square value of 105.474 with 1 degree of freedom and a p-value of 0.000. Since the p-value is less than 0.05, this result indicates that the model is statistically significant. This means governance factors meaningfully improve the model's ability to predict firm performance, confirming that they are relevant and significant predictors for firms listed at the Nairobi Securities Exchange.

Cook's Distance

From the results, the Cook's Distance values for the 181 observations showing a minimum of 0.00, a maximum of 0.57, and a mean of 0.02 with a standard deviation of 0.07. Since none of the Cook's Distance values exceed the commonly accepted threshold of 1.0, there is no indication of highly influential observations in the dataset. Therefore, the model is considered stable and reliable.

Wald Test

The Wald Test is used to assess the significance of individual predictors in the logit regression model. The results for the governance factors variable present a Wald statistic of 49.516 and a p-value of 0.000. This result is statistically significant ($p < 0.05$), indicating that governance factors are a strong and significant predictor of firm performance. Also, the constant term has a Wald statistic of 45.035 with a p-value of 0.000, indicating statistical significance. This means both the governance factors and the model intercept contribute meaningfully to the prediction of the dependent variable.

Regression Analysis Results*Model Summary*

The model incorporating governance factors successfully converged with a -2 Log Likelihood of 134.139, indicating proper specification, stability, and adequacy in explaining firm performance. The model summary is presented in Table 2. In addition, the Nagelkerke R Square value is 0.602, indicating that the model would explain 60.2% of the variation in the probability of firm performance being influenced by governance factors. This suggests that 39.8% of the variation in the probability of firm performance would be explained other factors other than environmental factors.

Table 2*Model Summary for Governance Factors and Performance of Listed Firms*

Step	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	134.139 ^a	.442	.602

a. Estimation terminated at iteration number 6 because parameter estimates changed by less than .001.

Variables in the Equation: In the logit regression output, the constant (-10.924) shows the baseline log-odds of firm performance when governance factors are zero. Its negative value indicates that, without contributions from governance factors, the likelihood of good performance is very low. In addition, the coefficient for governance factors is 3.072 with a standard error of 0.437, as shown in Table 3. This positive coefficient indicates that an increase in governance factors is associated with a higher likelihood of firm performance. The p-value for this coefficient is 0.000, which is below the 0.05 significance threshold, confirming that the relationship is statistically significant. The odds ratio is 21.591, meaning that for every one-unit increase in governance factors, the odds of a firm exhibiting high performance would increase by approximately 21.59 times.

Table 3*Variables in the Equation for Governance Factors and Performance of Listed Firms*

		B	S.E.	df	Sig.	Exp(B)	95% C.I. for EXP(B)	
							Lower	Upper
Step 1 ^a	Governance Factors	3.072	.437	1	.000	21.591	9.175	50.805
	Constant	-10.924	1.628	1	.000	.000		

a. Variable(s) entered on step 1: Governance Factors.

Discussion of Results

This research study established that governance factors positively and significantly influenced the performance of firms. The findings of this research study are in line with the observations by Faseha and Ghani (2022) who established that strong board oversight, transparent reporting, and robust internal controls significantly enhance firm performance by promoting effective management and accountability. The findings also concur with Mardini (2022) who established that sound governance practices strengthen decision-making processes, improve risk management, and enhance organizational credibility. The findings also support stakeholder theory, which argues that organizations should uphold transparency, fairness, and accountability in decision making to meet stakeholder expectations. However, the findings of this research study contradict Wang et al. (2021) who observed that certain governance mechanisms may create bureaucratic delays that hinder organizational responsiveness and slow down performance improvement efforts.

Conclusions and Recommendations

The research established that governance factors significantly influenced the performance of firms listed at the Nairobi Securities Exchange. The study therefore concludes that strong governance practices such as shareholders rights, risk management, ethical conduct, management quality and transparency and accountability play a critical role in enhancing firm performance. Therefore, the management of listed firms should institutionalize strong governance frameworks that emphasize transparency, shareholder rights, ethical conduct, and accountability. Boards must be diverse and effective, with clearly defined roles and regular evaluations. Firms should adopt international best practices, conduct governance audits, and treat governance as a strategic asset. Fairness in shareholder treatment, transparent communication strategies, and inclusive engagement forums are essential. Policymakers and regulators should ensure that all listed firms protect shareholder rights, particularly for minorities, by enforcing fair and inclusive governance structures.

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