EFFECTS OF AGENCY COSTS ON FINANCIAL PERFORMANCE OF COMPANIES LISTED AT THE NAIROBI SECURITIES EXCHANGE

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ABSTRACT

The purpose of this study was to establish the effects of agency costs on financial performance of companies listed at the Nairobi Securities exchange (NSE). In particular the study sought to investigate the effect of board independence, executive compensation, board size, free cash flows and chief executive duality on financial performance. Descriptive research design was adopted with target population being individuals working in the public listed companies in Kenya. The study used questionnaire as the primary tool to collect the required data while secondary data was sourced from published information about the current performance of the public listed companies and the implications resulting from the agency costs. The pilot study was conducted using questionnaires. Descriptive statistics such as means, standard deviation, frequency distribution and percentages were used to analyze the data. From the study we can conclude that firm's chief executive duality, executive remuneration, board independence, board size and free cash flow are all significant at 95 percent confidence level. This study reveals that, free cash flow is the most important in determining financial performance compared to other variables. Based onthe findings of this study, it can be revealed that, liquidity level of a firm is paramount in financial performance of any organization. Towards this end, the study recommends that organizations should consider form a lean but standard size board of director that would ensure efficiency in cash flow. The directors' compensations would translate to the amount of money flowing out in form of allowances and monthly compensations.

Key Words: *Effects, agency cost, financial performance, listed companies, Nairobi Security Exchange*

Introduction

Agency costs, which are manifest in various forms, are increasingly intrinsic in the modern day corporation, owing to the widening separation of ownership and control responsibilities, growing business diversification and segmentation across industry and business lines, and investor emphasis on near term performance and return outcomes. The adverse implications of these actions are then felt in the form of the destruction of shareholder wealth and wider impacts on other corporate stakeholders, such as debt providers, employees and society in general. The problems includeself-serving behavior on part of managers focused on status or empire building objectives, excessive prerequisite consumption, non-optimal investment decision-making or acts of accounting mismanagement or corporate fraud.Masulis*et al* (2008) analyzed the agency cost in U.S dual class companies and conclude that as the divergence widens at dual-class companies, corporate cash holdings are worth less to outside shareholders, chief executives receive higher levels of compensation, managers are more likely to make shareholder-value destroying acquisitions, and capital expenditures contribute less to shareholder value. These findings support the hypothesis that managers with greater control rights in excess of cash-flow rights are prone to waste corporate resources, thus negate performance.

The realization of the consequences flowing from the incidence of agency problems have led to emphasis being placed on importance of competitive markets for managerial labour and corporate control as monitoring mechanisms designed to limit the degree of agency divergence, the role of institutional shareholders as substitute agency devices and the development and enforcement of codes of corporate governance practice to enhance director and management oversight and create desirable incentive structures within firms.Academicians, however, examine the issue in order to find an answer for the dilemma from several different perspectives. For example, firms are proposed to improve their corporate governance and business ethics in order to reduce the self-interest motives of management and to avoid management's moral hazard, while agency theory examines how management's behavior could be directed at stockholder's interest by reducing agency cost. According to Brush, Bromiley, and Hendricks, agency theory holds based on three premises: First, the goal of management is to maximize his/her personal wealth instead of stockholder's wealth. Second, management's self-interest motivates waste and inefficiency in the presence of free cash flows. Third, agency costs are incurred to the burden of stockholders because of weak corporate governance.

Statement of the Problem

A survey by PricewaterhouseCoopers contends thatNational Human Resources Survey, Kenyan executives are among the highest paid employees in the world. The highest paid chief executive is earning Sh. 3.9 million in the financial sector while the lowest earns sh. 1.03m (PWC survey, 2009) While the survey which involved 110 organizations in both the private and public sectors, showed that the average remuneration of chief executive's across all sectors has increased by 30.7 percent since 2007 while the economy has grown by 1.7 percent and 7.1 percent, whereas

the company's profitability has not improved by the same margin; executive remuneration has outpaced companies' growth. According to the survey in 2007, the highest paid position was 315 times higher than the lowest paid while this year it is 414 times higher. The management positions were awarded an increment of 10.9 percent while the non-management positions were awarded 10.3 percent against an annual average inflation rate of 22.68 percent. The survey also projects an annual increment of 10.4 percent for management positions and 11.4 percent for non management positions in the 12 months since the last increment.

Further, despite the existence of a considerable literature on agency costs, all too frequently they remain poorly understood expenditures (Cuevas and Fischer 2006). The effects of agency costs have succeeded in being both common and yet little understood for the general public and the academic world alike. There are many reasons attributed to this phenomenon like the relationship between agency costs and the financial performance of a firm. This study, based on agency theory therefore aims to explore how agency costs affect firm performance with the data of Kenya publicly-listed companies. The study would like to empirically test how agency costs would affect firm performance by using the data of public-listed companies on Nairobi Securities Exchange (NSE).

Purpose of the Study

The purpose of this study was to establish the effects of agency costs on financial performance of companies listed at the Nairobi Securities exchange.

Objectives of the Study

The study was guided by the following objectives:

1. To investigate the effect of board independence on financial performance?
2. To determine the effect of executive compensation on financial performance?
3. To establish the effect of board size on financial performance?
4. To establish the relationship between free cash flows and financial performance?
5. To determine the effect of chief executive duality on financial performance?

Significance of the Study

Since the study was one of the few done on correlating agency costs and the financial performance of companies listed at the Nairobi Securities Exchange, it will be of immense benefit for future research and befitting purposes given that it will form part of empirical studies and academic knowledge will also draw from the same. The study by appraising the establishing the relationship between agency costs and the financial performance of companies listed at the

Nairobi securities exchange, it will be of use to the management of the companies and shareholders as it will act as an eye opener on whether agency costs incurred enhances or negates performance of the same.

Delimitations of the Study

The study was to establish the effects agency costs on financial performance of companies listed at the Nairobi Securities Exchange in Kenya. The study will focus more on effect of top management remuneration on operating costs of the companies, directors' fees, board independence and loans to directors. The researcher believes that this will provide an adequate and representative sample and would give reliable results or findings. The study will be carried out in the Nairobi County since nearly all companies are located in Nairobi.

Literature Review

Classens *et al* (2000) identify the pyramid structure and cross-holding as the major forms of such separation in eight East Asian economies since the separation of ownership and control in modern corporations gives rise to agency costs. They measure the agency costs by the divergence between the ultimate owner's cash flow rights and control rights and this has made their methodology of agency costs measurement be used extensively in scholarly work for example by Classens *et al* (2002), Lemmon and Lins (2003) use this methodology to examine the impact of agency costs on firm value in emerging economies. They conclude that in general, the divergence between the ultimate owner's cash flow rights and control rights has negative and significant impact on firm's value, as measured by Tobins Q.

In the Kenyan environment, the executive remuneration has not come under massive spotlight perhaps due to the nature of chief executive compensation. The Kenyan Companies Act sets the general framework for financial accounting and reporting by all registered companies in Kenya, and stipulates the basic minimum requirements with regard to financial reporting. Due to the limited details of the Act, financial reporting and regulation are supplemented by pronouncements of the Institute of Certified Public Accountants Kenya (Barako *et al.*, 2006).

CEO's Duality

Considerable degree of attention has been devoted to the critical role of boards ability in monitoring managers and removing non performing chief executive's. Jensen (1993) shows a deep concern that lack of independent leadership creates a difficulty for boards to respond to failure in top management. In this regard, Fama and Jensen (1983) also argue that concentration of decision management and decision control in one individual hinders boards' effectiveness in monitoring top management. It is argued that there is conflict of interests and higher agency costs when a chief executive doubles as the boar chair (Berg and Smith, 1978; Brickley *et al*.,

1997) and this leads to the proposition that the two positions be occupied by two persons. Nonetheless, there is also argument that when a chief executive doubles as board chair, it affords the chief executive opportunity to carry out decisions and projects without undue influence of bureaucratic structures and in this regard it is expected chief executive duality should have a positive relationship with performance (Rechner and Dalton, 1991). However, empirical evidence is not conclusive. Sanda *et al*., (2005) show a positive relationship between firm performance and separating the functions of chief executive and board chair. While Daily and Dalton (1992) find no relationship between chief executive duality and firm performance.

Directors remuneration

Agency theory ideals propose that higher management pay and or linkage monetary or share bonus or option entitlements to specific firm performance targets should act as a positive incentive mechanism, help in minimizing agency costs and aid in improving firm performance. Managerial remuneration and compensation structure has been discussed by Loderer and Martin, (1987) as well as Conyon, (1998).

Board size

As indicated by Jensen (1993), size is the value-relevant attribute of corporate boards in any organization. Organizational theory presupposes that larger groups take relatively longer time to make decisions and, therefore more input time (Steiner, 1972). What should a board size be? This has been a difficult question to answer because it seems to sit in the realms of relativity and subjectivity against the backdrop of unbiased objective measure. However, Lipton and Lorsch (1992) propose an optimal board size between 7-9 directors. In this respect, empirical studies have shown that the market values firms with relatively small board sizes (Sanda *et al*, 2005). Hence, as board size increases board activity is expected to increase to compensate for increasing process losses (Vafeas, 1999). The argument is that large boards are less effective and are easier for a chief executive to control. The cost of coordination and processing problems is also high in large boards and this makes decision taking difficult. On other hand, smaller boards reduce the possibility of free riding and therefore have the tendency of enhancing firm performance. We measure the size of the board by the number of directors serving on such boards**.**

Board independence

It is contended that NEDs may act as professional referees to ensure that competition among insiders stimulates actions consistent with shareholder value maximization (Fama, 1980). Weisbach (1998) and Cotter *et al (*1997) support this view underscoring the important role of outside directors in protecting shareholders' interests through effective decision control.

According to John and Senbet (1998), a board is more independent if it has more non-executive directors (NEDs). As to how this relates to firm performances, empirical results have been inconclusive. In one breadth, it is asserted that executive (inside) directors are more common with a firm's activities, and, therefore, are in a better position to monitor top management.

Some authors have also found that there is no significant relationship between proportion of NEDs and firm performance (Hermalin and Weisbach, 1991; Bhagat and Black, 2002). It has been shown that the effectiveness of a board depends on optimal mix of inside and outside directors (Fama and Jensen, 1983; Baysinger and Butler, 1985). However, available theory is scanty on determinants of optimal board composition (Weisbach, 2002). We measure the independence of the board by finding the ratio of NEDs to board size and we expect this to have a positive relationship with firm performance.

Board activity intensity

As argued by Vafeas (1999), the intensity of board activity isan important variable relevant to board attributes. *A priori*, the nature of the association between board activity intensity and firm performance is not clear. Some contend that board meetings are beneficial to shareholders. For instance Lipton and Lorsch (1992) propose that "the most widely shared problem directors face is lack of time to carry out their duties". In a similar argument, Conger *et al* (1998) propose that board meeting time is an important resource for improving the effectiveness of a corporate board. The implication is that when boards of directors meet frequently, they are likely to enhance firm performance and thus perform their duties in accordance with shareholders' interests. At the same time, it is believed that routine tasks absorb much of the meetings and this limits opportunities for NEDs to exercise meaningful control over management and therefore boards should be relatively inactive, and rather being more active when there are corporate crisis (Jensen, 1993). On contrary, some have argued that board meetings are not necessarily useful in that the limited time NEDs spend together is not used for meaningful exchange of ideas among themselves or with management (Vafeas, 1999).

This position has been recognized as a natural consequences of the fact that agenda setting for such meetings is done by chief executive officers (Jensen, 1993). In view of the debate surrounding board meetings and its relationship with firm performance, the significance of board activity intensity is an open question. We measure the intensity of board activity by the frequency of meetings annually.

Free Cash Flows

Free Cash Flows was originally proposed by Jensen (1993) who defined it as net cash flows after deducting the needs of positive NPV projects. Since Free Cash Flows is financial resources at the

management's discretion to allocate, it is also called idle cash flows. Jensen (1986) argued that too much Free Cash Flows would result in internal insufficiency and the waste of corporate resources, thus leading to agency costs as a burden of stockholder's wealth. According to Brush *et al* (2000) that weak corporate governance caused the inefficiency in the allocation of free cash flows since the corporate board of directors was directed at the policies in favour of management's interest at the expense of stockholders wealth.

In additional to Free Cash Flows, Jensen (1991) argued that the self-interest motive of management was an important factor leading to agency costs. This was especially obvious when stockholders and management interest were in conflict, and consequently stockholders interest was always dominated by management.

The Free Cash Flows hypothesis states that when a company has generated an excessive surplus of Free Cash Flows and there are not profitable investment opportunities available, management tends to abuse the Free Cash Flows in hands so as to resulting in an increase in agency costs, inefficient resource allocation and wrongful investment. Brush *et al* (2000) found that sales growth was most beneficial to companies being lack of cash flows but not necessarily to companies with sufficient Free Cash Flows and thus supported the Free Cash Flows hypothesis. Chung et al (2005) also found that excessive Free Cash Flows might have a negative impact on corporate profitability and stock valuation and thus proposed the control hypothesis of institutional investors.

Research Methodology

Research Design

Descriptive survey design was used.

Sampling Techniques and Sample Size

Subjects selected from the sampling frame form the units of observation in a study. The sampling frame of the study was the companies listed in the Nairobi Securities Exchange. The sample size of the study was 60 respondents who were divided into the various segments or industries in the NSE. The optimal size was used to fulfill the requirements of efficiency, representativeness and reliability which a simple size would not. Purposive sampling technique was adopted in this study since the respondents issued with the questionnaires were indentified beforehand to complete sample size.

Research Instruments

The study relied on use of a questionnaire as the primary tool to collect the required data from the target population. The target questions were designed carefully to ensure the respondents provided feedbacks to the anticipated questions and ensure the study is successful. The study

questions put in the questionnaires were based on ordinal scale for the purpose of ranking and measuring the data. The summated scale was adopted for scaling purposes to help come up with the best information from the study.

The study also considered the use of secondary data whereby there was published information about the current performance of the public listed companies and the implications resulting from the agency costs. The data was obtained from the Nairobi Securities Exchange and Capital Markets Authority website and offices based on company's annual reports regarding the macro-economic aspects and indicators of the economy. The information obtained was significant in helping in the study to highlight the major strategies and data for the study.

Data Analysis Methods

With the data having been collected, the filled-in questionnaires were coded to enable the responses to be grouped into various categories and entries made into Statistical Package for Social Sciences (SPSS version 17). Descriptive statistics such as means, standard deviation, frequency distribution and percentages were used to analyze the data. Tables and other graphical presentations as appropriate were used to present the data collected for ease of understanding and analysis. This generated quantitative reports through tabulations, percentages and measure of central tendency. Multiple regression analysis was conducted to determine the relationship between dependent and independent variables. The multiple linear regression was of the form:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \varepsilon$$

Whereby Y was ratings on financial performance; β_0 is the model's constant while β_1 to β_5 are the models coefficients; X_1 is the chief executive duality; X_2 is the executive remuneration; X_3 is the board independence; X_4 is the Board size and X_5 is the free cash flows. The study also made use of Pearson correlation analysis to determine if independent variables were linearly related with financial performance. The Pearson Product Moment correlation analysis was conducted at 95 percent confidence level.

Research Findings and Discussion

Research findings and discussions were based on research objectives which include the influence of board independence, executive compensation, board size, cash flows as well as chief executive duality on financial performance of companies listed in NSE.

Chief executive Duality, characteristics and remuneration

Table1: chief executive and chair of the board is the same person

	Frequency	Percent
Yes	2	4.1
No	47	95.9

Total	**49**	**100.0**

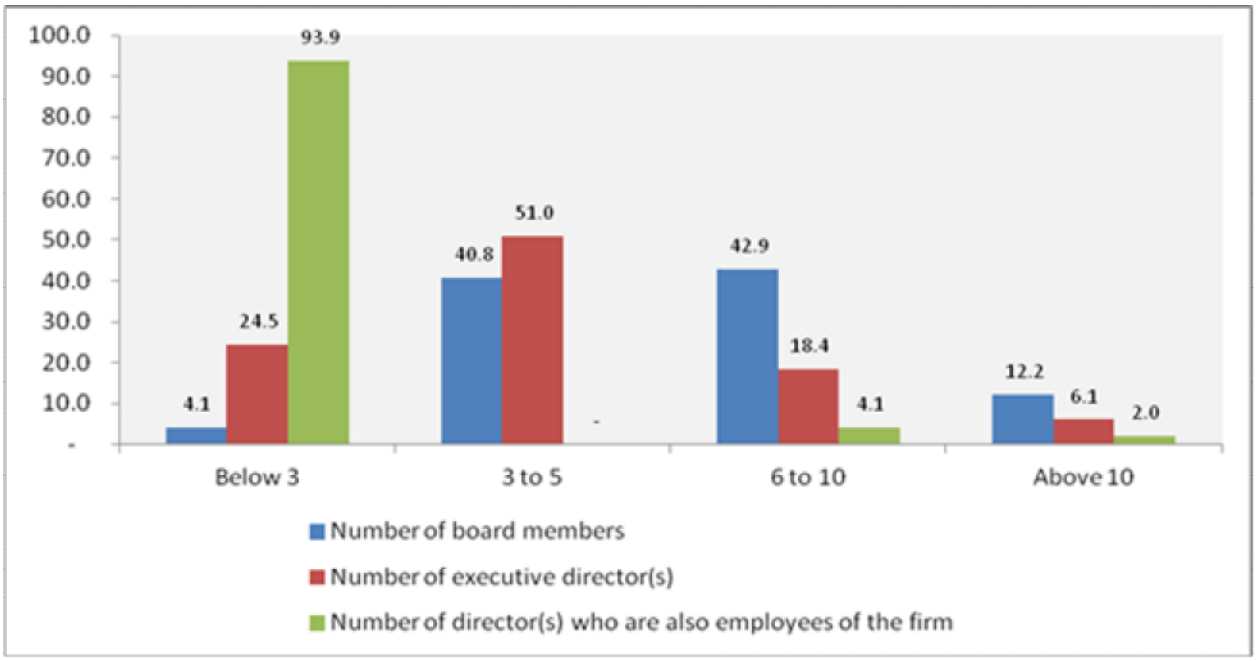
The respondents were also asked whether chief executive and chair of the board is the same person where an overwhelming majority of the respondents (95.9%) said not in their firms but 4.1 percent admitting that chief executive and chair of the board is one and the same person. This indicates that, to avoid the conflict of interests, the stewardship of the firms list in the NSE in the task of chief executive and that of chairmanship are separated.

Table2: chief executive duality weaken the monitoring role of the board in respondent's organization

	Frequency	Percent
Strongly Agree	21	42.9
Agree	12	24.5
Neutral	12	24.5
Disagree	3	6.1
Strongly disagree	1	2.0
Total	**49**	**100.0**

Board characteristics

Figure1: Board characteristics



Regarding the board characteristics in the respondent's respective firms, the study considered the number of board members, the number of executive director(s) as well as the number of director(s) who are also employees of the firm. From the findings most firms listed in NSE have at least 6 board members (55.1%), at most 5 executive director(s) (75.5%) and below 3 director(s) who are also employees of the firm (93.9%).

Table3: Tenure of board of directors

	Frequency	Percent
3 years and below	5	10.2
3 - 5 years	22	44.9
6 - 10 years	21	42.9
Over 10 years	1	2.0
Total	**49**	**100.0**

Concerning the tenure of board of directors, 44.9 percent have 3 - 5 years and 42.9 percent have 6 - 10 years. This implies that most firms listed at NSE have office tenure of at most 5 years.

Table4: Gender balance of the board of directors

	Frequency	Percent
Male	31	63.3
Female	18	36.7
Total	**49**	**100.0**

Concerning the gender balance of the board of directors, respondents said 63 percent are men while 37 percent are women. This indicates that there are more men than women in boards of directors for companies listed in the NSE.

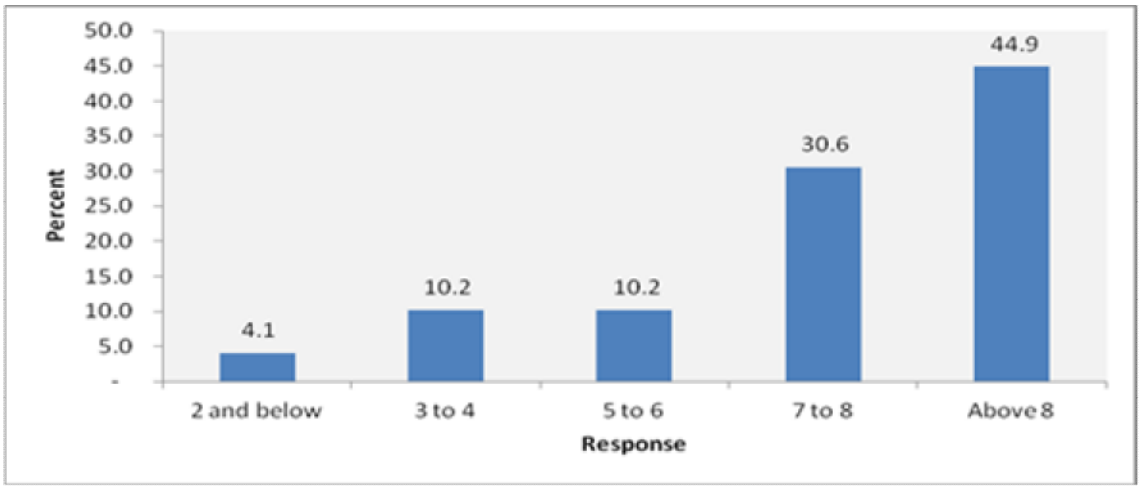
Table5: Age bracket of board members

	Frequency	Percent
Below 25 years	1	2.0
25 to 40 years	14	28.6
41 to 55 years	20	40.8
56 to 60 years	9	18.4
Above 60 years	5	10.2

Total	**49**	**100.0**

On age bracket of board members, the study revealed that, 40.8 percent are aged 41 to 55 years, 28.6 percent 25 to 40 years, and 18.4 percent 56 to 60 years while 10.2 percent are aged above 60 years. This implies that majority of members of boards for firms listed at NSE are over 40 years in age bracket. This could be explained by the fact that, the older the person, the higher the level of experience and thus higher chances of being selected as board member. At the same time, large portion of ownership of the companies listed in the NSE rests on hands of aged people, who are financially well thus investing more than their younger counterparts.

Figure2: Number of annual board meetings



Regarding the number of annual board meetings 44.9 percent of the respondents said Above 8, 30.6 percent said 7 to 8 while 10.2 percent mentioned 5 to 6. This implies that most firms listed in NSE have at least 7 board meetings per annum.

Table6: Respondent considers the board of directors to be independent

	Frequency	**Percent**
Strongly Agree	11	22.4
Agree	16	32.7
Neutral	8	16.3
Disagree	12	24.5
Strongly disagree	2	4.1
Total	**49**	**100.0**

On whether respondent considers the board of directors to be independent, 32.7 percent agreed while 22.4 percent strongly agree. This indicates that directors to the firms listed in NSE are considered to be independent.

Table7: The board independence influence firms performance

	Frequency	Percent
Strongly Agree	19	38.8
Agree	22	44.9
Neutral	2	4.1
Disagree	4	8.2
Strongly disagree	2	4.1
Total	**49**	**100.0**

Regarding respondents' opinion on whether the board independence influence firms performance, 44.9 percent agreed, 38.8 percent strongly agreed while only 4.1 percent strongly disagreed. This implies that the board independence influence firms performance.

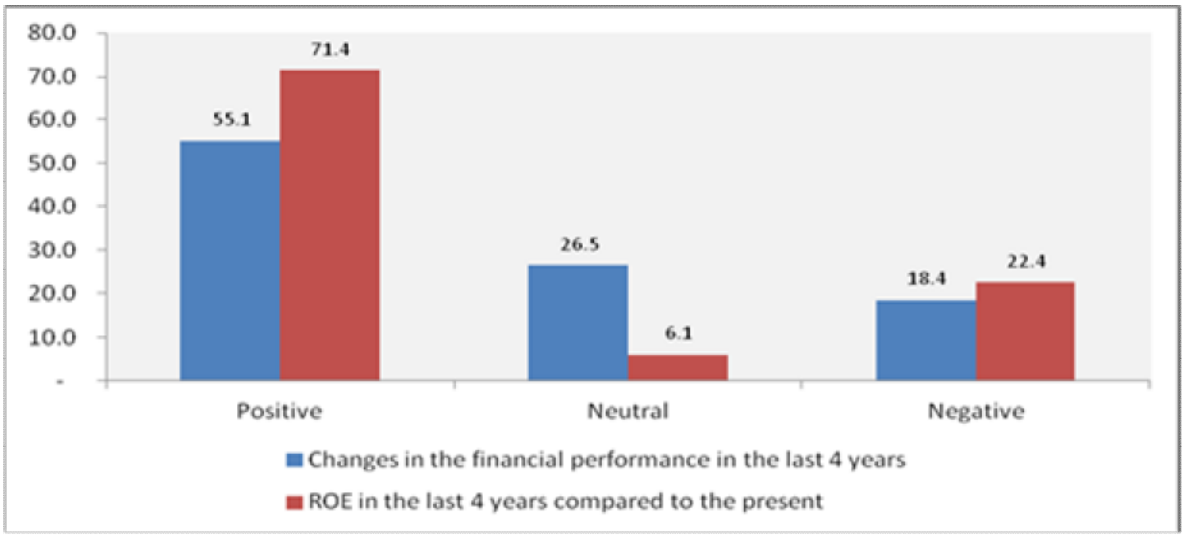
Financial performance

Table8: Company's return on equity generally exceeded its cost of equity

	Frequency	Percent
Strongly Agree	17	34.7
Agree	13	26.5
Neutral	5	10.2
Disagree	10	20.4
Strongly disagree	4	8.2
Total	**49**	**100.0**

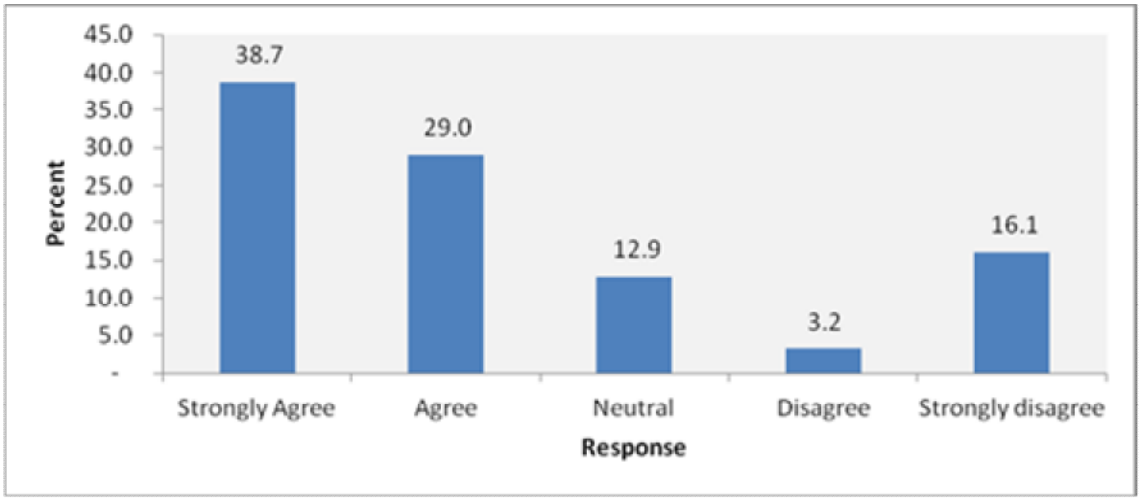
From the findings, 34.7 percent of respondents strongly agreed, 26.5 percent agree, 20.4 percent disagreed while 8.2 percent strongly disagreed.

Figure3: Financial performance in the last 4 years



Concerning the company's financial performance in the last 4 years, the researcher considered changes in the financial performance in the last 4 years and the ROE in the last 4 years compared to the present. On changes in the financial performance in the last 4 years, 55.1 percent said changes were positive with 18.4 percent saying they are negative. Regarding ROE in the last 4 years compared to the present, 71.4 percent said the changes were positive while 22.4 percent said it was negative. This indicates that for most of the firms listed in NSE, their respective financial performance and ROE have been positive for the last 4 years.

Figure4: Cash flows have any influence on investment decisions and affect financial performance



On whether cash flows have any influence on investment decisions and affect financial performance 38.7 percent agreed strongly, 29.0 percent agreed, while 12.9 percent were neutral. This indicates that cash flows have great influence on investment decisions which affect financial performance.

Inferential findings

Correlation coefficients

Table9: Correlation coefficients

	Standardized coefficients		
	B	Beta	Sig
Constant	0.55		0.031
chief executive duality	0.39	0.48	0.048
Executive remuneration	0.31	0.63	0.001
Board independence	0.31	0.51	0.004
Board size	0.48	0.59	0.002
Free cash flow	0.56	0.72	0.001

Table13 illustrates the analytical coefficients for the variable relations. The researcher considered five variables to be significantly influencing financial performance which included the firm's chief executive duality, executive remuneration, board independence, board size and free cash flow. The study revealed that the most prevalent factor among the five mentioned was free cash flow with beta value of 0.72 while board independence, executive remuneration, chief executive duality and board size had beta value of 0.51, 0.63, 0.48 and 0.59 respectively. The significant level was 5 percent implying that, the higher the significant level for an explanatory variable, the lower the confidence level and thus the less the variable explains changes in the dependent variable. Since all the five variables had a significant level of less than 0.05, it implies that at 95 percent confidence level, the researcher was confidence that all the five explanatory variables (elements of agency costs) considered had significant impact on financial performance of firms listed in the NSE. The analytical model has an autonomy value of 0.55 while probabilistic values were 0.48 for chief executive duality, 0.48 for executive remuneration, 0.63 for board independence, 0.59 for board size and 0.19 for free cash flow.

Given that $Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4+\beta_5X_5 + \varepsilon$

Whereby Y is ratings on financial performance; β_0 is the model's constant while β_1 to β_5 are the models coefficients; X_1 is the chief executive duality; X_2 is the executive remuneration; X_3 is the board independence; X_4 is the Board size and X_5 is the free cash flows. The study will also make use of Pearson correlation analysis to determine if independent variables are linearly related with

financial performance. The Pearson Product Moment correlation analysis will be conducted at 95 percent confidence level.

The model can then be generated as follows:

$$\mathbf{Y = 0.55 + 0.48X_1 + 0.63X_2 + 0.51X_3 + 0.59X_4 + 0.72X_5 + \varepsilon}$$

From the model, the constant value of 0.55 implies that the level of financial performance in firms listed in NSE will have an index of 0.55 when coefficients for all variable factors are zero. At the same time, change in executive remuneration, board independence, board size and free cash flow by 1 unit in each, will result to a positive change in financial performance by 63 percent, 51 percent, 59 percent and 72 percent respectively. This is an indication that the five independent variables under investigation were positively related to the dependent variable (financial performance).

Coefficient of determination

Table10: Multivariate R-Square

Model Summary									
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	0.89	0.79	0.67	0.24	0.79	18.10	5	43	0.000

Predictors: (Constant), Free cash flow, chief executive duality, Executive remuneration, Board size, Board independence

R^2 is called the coefficient of determination and tells us the proportion of the change in financial performance that is caused by the change in explanatory variables. From Table14, the value of R square was found to be 0.79 indicating that chief executive duality, executive remuneration, board independence, board size and free cash flow explained 79 percent of any change in financial performance of firms listed in NSE. When F is greater than 1, the set of explanatory variables is considered to be significantly determining any changes in financial performance.

Level of significance

To determine the level of significance of the different explanatory variables, the researcher considered the t value(s) as well as the $R^{2.}$ Table15 indicates both the t value and R^2 for each explanatory variable analyzed as a bi-variant.

a) R^2

Table11: Bi-variate T-Ratio and R-Square

	T-Value	R-Squared
chief executive duality	3.06	0.54
Executive remuneration	4.67	0.67
Board independence	5.10	0.61
Board size	4.52	0.76
Free cash flow	9.26	0.80

Table23 shows that free cash flow carried the highest weight in explaining factors that affect financial performance with an index of 80 percent. Other factors which included board independence, executive remuneration, board size and chief executive duality had explanation weight of 61 percent, 67 percent, 76 percent and 54 percent respectively.

T-Ratio (t)

This is also called the student ratio and tells us the statistical significance of the explanatory variables. If t >2, the explanatory variable is said to be statistically significant. The opposite is true if t <2.Regarding the statistical significance of the explanatory variable towards the financial performance, the researcher took a general assumption that those variables with a student ratio greater than two (2) were highly significant and therefore relevant in determining financial performance. Free cash flow was found to be the most statistically significant with T-Value of 9.26 while board independence, executive remuneration, board size and chief executive duality had statistical significance of 5.10, 4.67, 4.52 and 3.06 respectively. Details of the same are as shown by Table23

To determine the degree of relationship between the explanatory variables, the researcher performed a Pearson's moment correlation as illustrated by Table24. Pearson's correlation coefficient (r) is a measure of the strength of the association between the two variables. This enabled the researcher to establish the level to which one variable moved together with the other in explaining changes in financial performance. Findings indicate that, the relationship between all the variables (that is, chief executive duality, Executive remuneration, Board independence, Board size, free cash flow as well as financial performance) with each other is significant since the significance level at 95 percent confidence level; one tail test is less than 0.05.

Highest correlation was found between free cash flow and financial performance with coefficient factor of 0.77. Others were free cash flow and executive remuneration, financial performance and board independence, free cash flow and board independence as well as free cash flow and board size with each a correlation coefficient of 0.55, 0.19, 0.59, 0.59 respectively. Board independence and executive remuneration were also found to be correlating highly with correlation coefficient of 0.55 while board size was also found to be correlating highly with board independence (0.19). Least correlation was identified between free cash flow and chief executive duality.

The results indicate that, with vast employment of free cash flow, chief executive duality will insignificantly affect the success of financial performance. Free cash flow is particularly generation of an organization's overall objective(s), principles and tactics relating to the agency cost for a particular firm. This implies that the degree of substitutability was highest for free cash flow and financial performance and lowest for free cash flow and chief executive duality.

Conclusions

From the study we can conclude that firm's chief executive duality, executive remuneration, board independence, board size and free cash flow are all significant at 95 percent confidence level. This is because the significance level for 1-tail test showed that, each independent variable

has a significance value of less than 0.05, an indication that the researcher was over 95 percent confidence that chief executive duality, executive remuneration, board independence, board size and free cash flow significantly influence financial performance of a firm. Even though all these variables affect financial performance of a firm, this study reveals that, free cash flow is the most important in determining financial performance compared to other variables. This was confirmed by the findings that 80 percent of any change in financial performance is explained by the level of free cash flow at bi-variate level.

Other factors that are equally significant include the size of the board of directors. This is because the larger the size of the board the directors, the higher the expenses on emoluments and thus the lower the liquidity of a firm. This, together with the amount of free cash flow translates to financial performance. These emoluments are limited to cash compensation as share option issues have not come into play yet as such the NSE disclosure on shares is limited to bonus and rights issues to the general investing public.

Recommendations

Based on findings of this study, it can be revealed that, liquidity level of a firm is paramount in financial performance of any organization. Towards this end, the study recommends that:

1. Organizations should consider form a lean but standard size board of director that would ensure efficiency in cash flow. The directors' compensations would translate to the amount of money flowing out in form of allowances and monthly compensations.
2. Firms listed in the stock market should also consider managing their free cash flow through rewarding their board of directors by allocating shares and thus improving on liquidity level of a company.
3. Even though firms should endevour boosting their financial performance through leveraging the cash flow, higher management pay and or linkage monetary or share bonus or option entitlements to specific firm performance targets should act as a positive incentive mechanism, help in minimizing agency costs and aid in improving firm performance.

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