EFFECTS OF BOARD CHARACTERISTICS ON FINANCIAL PERFOMANCE OF NON GOVERMENTAL SECTOR IN KENYA : A CASE OF THE INTERNATIONAL PLANNED PARENTHOOD FEDERATION

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ABSTRACT

NGO sector in both developed and developing countries has experienced exponential growth, characterized by donor and development partners' preference to channel aid through NGOs as they are considered to deliver services better than governments coupled with their flexibility and innovation. However, their governance are influenced by financial management crisis; lack of a stable and diverse funding base; leadership crisis, Competition with other organizations with similar interests and dwindling relevance and lack of focus. IPPF like any other NGO is not excluded from such challenges. This study therefore sought to assess the effects of board characteristics on financial performance among NGO in Kenya with International Planned Parenthood Federation (IPPF) being our case study. The specific objective deemed to assist achieving the main objective included: to assess the effect of board size, board composition, board structure and Board meetings on financial performance of IPPF. Using both stratified and purposive sampling techniques, data was collected from regional secretariat staff, volunteers, and member association staff (country office staff) to sample total sample of 54 respondents form a population of 180 individuals. Both interview and questionnaire were used to collect data. The data collected was summarized and analyzed with both descriptive and inferential using Statistical Package for Social Science (SPSS) Version 20. The study found out that board size and financial performance were positively and significantly related (r=0.016, p=0.032). Board composition and financial performance were positively and significantly related (r=0.019, p=0.020). It was further established that board structure and financial performance were positively and significantly related (r=0.18, p=0.022), while board meetings and financial performance were positively and significantly related (r=0.25, p=0.010). Based on the findings above the study concluded board size, board composition, board structure and board meetings have a positive and a significant effect on financial performance. The study recommended for a good representation of women in the board. In addition, the study recommended for a board that includes non-board members on the committees of the boards and inclusion of major donors on the board .Further, the study recommended for a standard frequency of board meetings. Lastly, the study recommended for the directors to also participate in the board meetings.

Keywords: Board size, Board meetings, Board structure, Board composition, financial performance, IPPF

INTRODUCTION

Background and Research Gap

The absence of good Corporate Governance is a major cause of failure of many well performing companies. Existing literature generally support the position that good Corporate Governance has a positive impact on organizational performance; OECD (2009), Gompers, Ishii and Metrick (2003), Claessens, Djankov and Fan (2002) and others. The economic well-being of a nation is the reflection of the performance of its companies. Thus the low level of development of developing nations is attributed to the low level of good Board characteristics. Hence the emphasis placed on good Corporate Governance in the existing literature as the most important problem facing the development of countries, such as Kenya.

Empirical studies have provided the nexus between corporate governance and firm performance. Bebchuk, Cohen, and Ferrell (2004) indicate that well-governed firms have higher firm performance. Research has also shown that there is a strong link between the performance of corporations and the governance practices of their boards (Gregg, 2001; Kiel & Nicholson, 2002). Similarly a study carried out in the United States by Gompers, Ishii and Metrick (2003) found a strong correlation between good board characteristics and superior shareholder performance. The study also revealed that two-thirds of investors were prepared to pay more for shares of companies that had good board characteristics. The absence of competent governance structures and processes hampers the development of both individual organizations as well as the sector as a whole. Non-profit boards face a tough challenge in that they oversee the performance of a single entity and at the same time are accountable to a larger public that is difficult to define (Wyatt, 2002). There is a growing need for NGOs throughout the world to be more effective and productive and one of the many ways they are achieving this is by broadening and strengthening the constitution of their boards (Mostashari, 2005).

Muriithi (2008) in his study on the relationship between board characteristics and performance in the New Kenya Cooperative Creameries concluded that the adoption of corporate government practices that had also developed over time had in fact improved the company’s performance. In Kenya, previous studies conducted in the area of corporate governance and performances have concentrated on the profit making organizations. Mulili (2010) examined the concept of board characteristics from a historical perspective and explored how the agency theory and stewardship theory affect board characteristics focusing on the universities in Kenya. Mwangi (2006) conducted a study on integrated governance and provision of quality healthcare in non-profit institutions and focused on Gertrude's Children's Hospital. Zietlow et al., (2007) states that the success of a NGO is dependent on its workforce and governing body and structure it assembles to accomplish its mission. They go ahead to mention four key attributes for NGOs: ethics, governance, transparency and the constant building of trust. One of the key issues that motivate the importance of governance, structure, accountability and ethics is vulnerability to fraud. This provides justification for the current study.

Statement of the Problem

IPPF is 100% dependent on donor funding and operating in a competitive environment where organizations with similar interest are competing for the scarce resources. Over the past 60 years IPPF have been receiving unrestricted funds from its donors in which there were no restrictions on the usability of these funds. However, the donor funding has since changed from unrestricted funds to restricted funds where the funds are now received with restrictions on the usability and accountability of such funds, resulting to high demand for accountability and donors wanting value for their money. There is scanty information on whether these changes in category of funding has led to changes in board characteristics and thus financial performance (IPPF report 2009). Despite of this, IPPF costs of running board meetings have increased from USD ($)89,000 in 2010 to USD ($) 268,000 in 2014(IPPF report 2014).Despite increase in the number of board members and cost of running the board it is not clear on how this increase has impacted on efficiency and effectiveness and therefore overall organizations financial performances. This study therefore sought to narrow the gap by assessing the effects of board characteristics on financial performance of IPPF.

Scholars have noted several factors affecting board governance and thus performance. Owino (2013) established negative relationship between board size and organization's financial performance; Sozi (2013) established board performance is positively correlated to effectiveness of the board and effectiveness of board was found affected by board composition and quality, size of board, board diversity, information asymmetries and board culture. Based on the extensive literature, three board characteristics (board composition, board size, and board structure and board meetings) have been identified as possibly having an effect on financial performance and these characteristics are set as the independent variables. As such, the study sought to assess the effect of board size, structure, composition and accountability on financial performance of International Planned Parenthood Federation.

Objectives of the Study

i. To assess the extent to which board size affect financial performance of IPPF.
ii. To determine the effect of board composition on financial performance of IPPF.
iii. To evaluate the effect of Board Structure on financial performance of IPPF.
iv. To find out the extent to which board meetings affect financial performance of IPPF.

LITERATURE REVIEW

Theoretical Review

Agency theory

The 1976 article, “Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure” by Jensen and Meckling helped establish agency theory as the dominant theoretical framework of the corporate governance literature and position shareholders as the main stakeholder (Lan*et al.,* 2010 and Daily *et al*., 2003). Jensen and Meckling (1976) further define agency relationship as a contract where one or more persons (principal) engage other person (agent) to perform some service on their behalf, which involves delegating some decision-making authority to the agent’. The scenario normally generates a conflict of interests.

Principal-agent theory encapsulates a tradition of rational choice modelling, in which some actor(s) (the principal(s)) uses whatever actions are available, to provide incentives for some other actor(s) (the agent(s)) to make decisions that the principal most prefers. Principal-agent theory has become a widely used paradigm for analyzing public accountability. Public accountability is a function of the capabilities of principals to judge the performance of their agents (Achen and Bartels 2002; Healy and Malhotra 2010; Lenz 2012; Lupia and McCubbins 1998). But it is also in part a function of institutions themselves. The traditional shareholder perspective asserts that the exclusive focus of corporate governance should be to maximize shareholder value. If the goal of maximizing shareholder wealth conflicts with the interests of other groups, those other interests should be ignored, unless certain laws and regulations mandate the management to consider those (Macey & O’Hara, 2003).

Agency theory is relevant to this study since it informs the independent variables that is board characteristics. Board members are the agents of the company therefore they are expected to up hold the interests of the firm rather than their own interests.

Empirical Literature Review

A study by Beiner, Drobetz, Schmid and Zimmerman (2004) reviewed the Corporate Governance and firm valuation by using a broad Corporate Governance index and additional variables related to ownership structure, board characteristics, and leverage to provide a comprehensive description of firm-level Corporate Governance for a broad sample of Swiss firms. The study found out that an increase in Corporate Governance index by one point caused an increase of the market capitalization by roughly 8.6%, on average, of a company’s book asset value. Zheka (2007) in his study found out that a one-point-increase in the corporate governance index results in around 0.4%-1.9% increase in performance; and a worst to best change predicts a 40% increase in company’s performance. Using data on companies in many African countries, including Ghana, South Africa, Nigeria and Kenya, Kyereboah-Coleman (2007) indicated that better governance practices are associated with higher valuations and better operating performance. Baker, Godridge, Gottesman and Morey (2007) using a unique dataset from Alliance Bernstein, an international asset management company, with monthly firm-level and country-level governance ratings for 22 emerging markets countries over a five year period, report a significantly positive relation between firm-level (and country-level) Corporate Governance ratings and market valuation, suggesting lower cost of equity for better governed firms.

In Kenya, Wanjiku et al., (2011) carried out a study to establish the Board characteristics of firms and its relationship with the growth of Companies listed at the Nairobi Securities Exchange using a causal comparative research design. The study focused on corporate communication, leadership and technology application. The study found a positive linear dependence of growth and Corporate Governance. Ongore and K'Obonyo (2011) conducted a similar study in Kenya to examine the interrelations among ownership, board and manager characteristics and firm performance in a sample of 54 firms listed at the Nairobi Securities Exchange and the study indicated a positive relationship between managerial and firms performance.

Booth, Cornett and Tehranian (2002) compare the 100 largest banks to the 100 largest industrial Örms in 1999 and Önd that they have larger boards with a greater proportion of outsiders. Adams and Mehran (2003) and that bank boards are larger and more independent over the period 1986-1999 using a sample of 35 large bank holding companies and data on large manufacturing Örms from Yermack (1996), amongst others. Adams (2011) finds that bank boards are larger and more independent than non-financial firms in the risk metrics database of S&P 1500 firms from 1996-2007. Clark (2002) argued that serving on a board requires significant time and attention on the part of directors. They must participate in board meetings, review relevant materials, serve on board committees, and prepare for meetings and discussions with management. In addition, directors must spend the time needed and meet as frequently as necessary to properly discharge their responsibilities.

RESEARCH METHODOLOGY

The study adopted a descriptive survey design. Descriptive research design was chosen because it enabled the study to generalise the findings to a larger population. The target population of the study included country office staff, Regional office staff, Regional Secretariat staff, Youth and Adult. These were 180 in total. The study adopted stratified sampling technique to select the sample for the study. Purposive sampling was also applied to select the member associations (country offices) based on language, management challenges and successes. The key members of Senior Management Team (SMT) were interviewed from each MA. At regional level the selection of key respondents was purposive based on management hierarchy of the regional secretariat. The study used 30% of the population in each population stratum thus the total respondents were 54.

This study utilized questionnaire as the data collection instrument. Data analysis was through both descriptive and inferential statistics. Descriptive statistics that were utilized include percentages, mean scores and frequency distributions. These were utilized to enable a description of the various data that was collected. Inferential statistics that were utilized include regression and correlation analysis. Regression analysis was applied to perform the t and f-tests that assisted in establishing the effect of corporate governance indicators on financial performance of IPPF. The model utilized was presented below;

$\mathbf{Y} = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + E$ Where :-

Y =Financial Performance (Dependent variable)

$\beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4$= Explained Variations of the Model.

α =constant. It defines the level of financial performance without inclusion of predator variables

E = Unexplained Variation i.e. error term

X1 = Board Size

X2 = Board Composition

X3 = Board Structure

X4 = Board Meetings

β0 = Constant. It defines the level of financial performance without inclusion of predictor variables.

β1, β2, β3, β4, = Regression Co-efficient. Define the amount by which Y is changed for every unit change of predictor variables.

RESEARCH FINDINGS AND DISCUSSION

The number of questionnaires that were administered was 51. A total of 54 questionnaires were properly filled and returned. This represented an overall successful response rate of 94.44% as shown on Table 1.

Table 1: Response Rate

Response	Frequency	Percent
Returned	51	94.44%
Unreturned	3	5.56%
Total	**54**	**100%**

Descriptive Statistics

Financial Performance

The dependent variable under this study was financial performance. Figure 1 shows the funds raised both restricted and unrestricted funds less the expenditure for the year 2010 to 2014 in IPPF. For the year 2010, the funds which remained after deducting all the expenditures were 2,308,378, for the year 2011 the surplus funds were768, 984. In the year 2012, the remained funds was 1,205,964 while for the year 2013 and 2014 were 509,926 and 1,523,283 respectively as shown in figure 4.2.This implies that for the last five years IPPF has been working on surpluses and this is an indication of good financial performance.

A fund raised less expenditure was found to be a good measure for the financial performance of IPPF which is a non-profit making organization. This is consistent with Epstein & McFarlan, (2011) who argued that the non-profit entities devote a significant time basing their performance on financial metrics; funds raised and budget achievement. Though this measure is important, the core business of the organization should first be realized through aligning this to the goals of the organization.

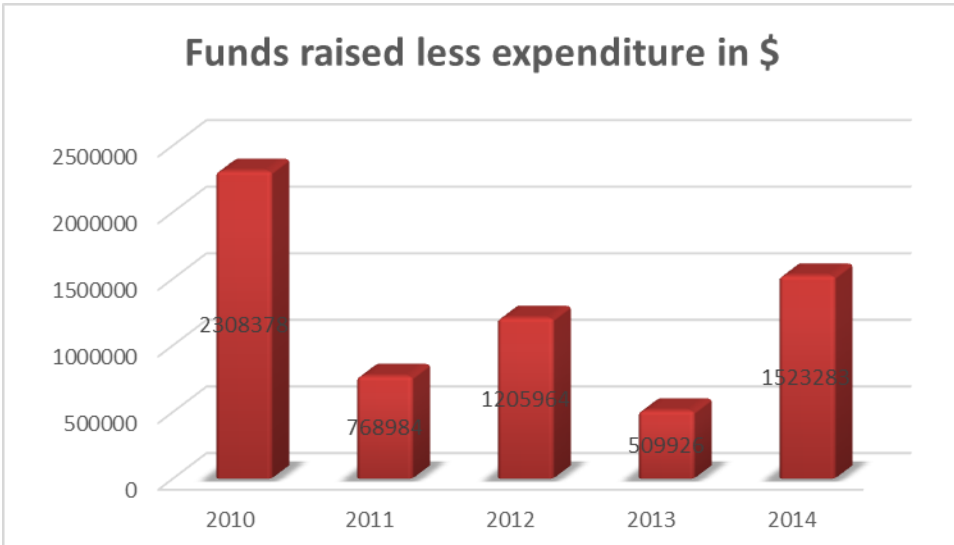

Figure 1: funds less the expenditure for the year 2010 to 2014

Board size

Table 2 shows the number of board members for IPPF for the year 2010 to 2014. The board members in each year include both adult and youth volunteers. In the year 2014, the board members were 133 while in the year 2013 they were 129. In the year 2012 they were 121 while in the year 2011 and 2010 they were 102 and 98 respectively. It is evident that the number of board members in IPPF has been on the rise for the last 5 years due to increased membership of countries to IPPF federation. Results are presented in Table 2.

Table 2: Board Members

Year	Number of Board members
2014	133
2013	129
2012	121
2011	102
2010	98

Board Composition

Table 3 shows the percentage of women and male representation in the board. The results show that in the year 2014 percentage of female representation was 55% and male 45% of the total board members while in the year 2013 they were 40% female and 60% male. In the year 2012 they were 52% female and 48% male while in 2011 and 2010 they were 46% female and 54% male and 50% both male and female respectively. This means that there is a good representation of women in IPPF board, this describe the good gender equality of the board. There is no donor presentation as well as outside directors in the board implying that the board comprise of only internal directors.

Table 3: Board Composition

Year	Female%	Male %
2014	55	45
2013	40	60
2012	52	48
2011	46	54
2010	50	50

Board Structure

The respondents were asked to respond on the statements on board structure. The responses were rated on a five likert scale as presented in Table 4. Majority of 78.4%(45.10%+33.3%) of the respondents agreed with the statement that There is diversity in the board –age/gender, 68.7% agreed with the statement that board of members are professionals, 68.7% of the respondents agreed that board of members have job experience of their position, 78.5% of the respondents agreed that Board plays oversight role such as active monitoring of management and resolve internal conflicts, 85.3% of the respondents agreed that there is a well-defined succession plan while 70.6% of the respondents agreed There is division of responsibilities of chairperson and CEO. On a five point scale, the average mean of the responses was 3.87 which mean that majority of the respondents were agreeing with most of the statements; however the answers were varied as shown by a standard deviation of 1.08.

This finding is consistent with that of Callen *et al* (2010) who suggested a structure of the board that includes non-board members on the committees of the boards and inclusion of major donors on the board. This they contend would make corporate governance stronger for a non-profit organization and enhance monitoring of the activities of the management by the board. They further suggest a clear structure that would ensure separate roles between the board and the management. Leblanc and Lindsay (2010) observe the document that establishes a non-profit entity prescribes the size of the board, the tenure of members of the board, and other requirements like geographical representation or ex-officio positions where applicable.

Table 4: Board structure

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean	Std. Dev.
There is diversity in the board –age/gender	3.90%	5.90%	11.80%	45.10%	33.30%	3.98	1.029
Board of members are professionals	5.90%	9.80%	15.70%	37.30%	31.40%	3.78	1.172
Board of members have job experience of their position	9.80%	5.90%	15.70%	41.20%	27.50%	3.71	1.221
Board plays oversight role such as active monitoring of management and resolve internal conflicts	5.90%	9.80%	5.90%	51.00%	27.50%	3.84	1.12
There is a well-defined succession plan	0.00%	9.80%	5.90%	33.30%	51.00%	4.25	0.956
There is division of responsibilities of chairperson and CEO	5.90%	5.90%	17.60%	58.80%	11.80%	3.65	0.976
Average						**3.87**	**1.08**

Board Meetings

Table 5 shows the number of meetings held in IPPF for the last five years. The results revealed that there were 5 meetings in 2014 and 3 meetings in 2013.In the year 2012 there were 4 meetings while the year 2011 and 2010 they were 3 and 4 meetings respectively

Table 5: Number of meetings

year	Number of board meetings
2014	5
2013	3
2012	4
2011	3
2010	4

Inferential Statistics

The inferential statistics presented on this section were overall correlation analysis, model fitness, analysis of variance and regression of coefficients.

Overall correlation analysis

Correlation analysis is the statistical tool that can be utilized to determine the level of association between two variables (Levin & Rubin, 1998). This analysis can be seen as the initial step in statistical modelling to determine the relationship between the dependent and independent variables. Prior to carrying out a multiple regression analysis, a correlation matrix was developed to analyze the relationships between the independent variables as this would assist in developing a prediction multiple model which will reveal no relationship in cases where the value of the correlation is 0. On the other hand, a correlation of ±1.0 means there is a perfect positive or negative relationship (Hair et al., 2010). The values are interpreted between 0 (no relationship) and 1 (perfect relationship). Also, the relationship is considered small when $r = \pm 0.1$ to ± 0.29, while the relationship is considered medium when $r = \pm 0.30$ to ± 0.49, and when r is ± 0.50 and above, the relationship can be considered strong.

Table 6 below presents the results of the correlation analysis. The results indicated that there was a positive and a significant association between board size and financial performance ($r=0.177$, $p=0.0215$).This means that an increase in board size will lead to an increase in financial performance. In addition, the results revealed that there was a positive and a significant association between board composition and financial performance ($r=0.343$, $p=0.014$).This means that an increase in the board mix will lead to an increase in the financial performance. The results indicated that there was a positive and a significant association between board structure and financial performance ($r=0.305$, $p=0.030$).This means that an improvement in board structure will lead to an increase in the financial performance. Further, correlation analysis showed a positive and a significant relationship between board meetings and financial performance($r=0.376$, $p=0.006$).This means that an increase in the number of board meetings will lead to an increase in the financial performance.

These findings agree with that of Chaganti *et al.* (1985) who investigated the differences in board size of 21 pairs of failed and non-failed retailing firms in the USA during 1970-1976. They found that failed 74 firms tended to have smaller boards than non-failed ones, showing that companies with a larger board size would perform better than those with a small board, and companies with larger boards have greater chances of survival.

Table 6: Overall correlation matrix results

		Financial performance	Board size	Board composition	Board structure	Board meetings
Financial performance	Pearson Correlation	1.000				
	Sig. (2-tailed)					
Board size	Pearson Correlation	0.177	1.000			
	Sig. (2-tailed)	**0.0215**				
Board composition	Pearson Correlation	.343*	-0.207	1.000		
	Sig. (2-tailed)	**0.014**	0.145			
Board structure	Pearson Correlation	.305*	.428**	0.164	1.000	
	Sig. (2-tailed)	**0.030**	0.002	0.251		
Board meetings	Pearson Correlation	.376**	0.071	0.084	0.051	1.000
	Sig. (2-tailed)	**0.006**	0.623	0.558	0.722	

* Correlation is significant at the 0.05 level (2-tailed).

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

Multivariate Regression Analysis

The results presented in table 7 present the fitness of model used of the regression model in explaining the study phenomena. Board size, board composition, board structure and board meetings were found to be satisfactory variables in explaining financial performance. This is supported by coefficient of determination also known as the R square of 55.8%. This means Board size, board composition, board structure and board meetings explain 55.8% of the variations in the dependent variable which is financial performance. This results further means that the model applied to link the relationship of the variables was satisfactory.

Table 7: Model Fitness

Indicator	Coefficient
R	0.746
R Square	0.558
Adjusted R Square	0.252
Std. Error of the Estimate	0.4078162

In statistics significance testing the p-value indicates the level of relation of the independent variable to the dependent variable. If the significance number found is less than the critical value also known as the probability value (p) which is statistically set at 0.05, then the conclusion would be that the model is significant in explaining the relationship; else the model would be regarded as non-significant.

Table 8 provides the results on the analysis of the variance (ANOVA). The results indicate that the overall model was statistically significant. Further, the results imply that the independent variables are good predictors of performance. This was supported by an F statistic of 5.211 and the reported p value (0.002) which was less than the conventional probability of 0.05 significance level.

Table 8: Analysis of Variance

	Sum of Squares	df	Mean Square	F	Sig.
Regression	3.466	4	0.867	5.211	**0.002**
Residual	7.65	46	0.166		
Total	11.117	50			

Regression of coefficients results in table 9 shows that board size and financial performance are positively and significantly related (r=0.016, p=0.032). The table further indicates that board composition and financial performance are positively and significantly related (r=0.019, p=0.020). It was further established that board structure and financial performance were positively and significantly related (r=0.18, p=0.022), while board meetings and financial performance were positively and significantly related (r=0.25, p=0.010).

Table 9: Regression of Coefficient

Variable	B	Std. Error	t	sig
(Constant)	0.714	0.8	0.892	0.377
Board size	0.016	0.006	2.01	0.032
Board composition	0.019	0.008	2.415	0.020

Board structure	0.18	0.146	2.236	0.022
Board meetings	0.25	0.093	2.683	0.010

The specific model was;

Financial Performance =0.714+0.016 X1 +0.019X2 +0.18 X3 +0.25 X4

Where;

X1 =Board size

X2 =Board composition

X3 =Board structure

X4=Board meetings

Conclusion

The objective of this research was to examine the effect of board characteristics on financial performance of IPPF. With regards to the examination of the effect of board characteristics on financial performance, linear regression and Pearson's correlation analysis were used. Based on the findings above the study concluded board size, board composition, board structure and board meetings have a positive and a significant effect on financial performance. The study also concluded that board size and financial performance are positively and significantly related. This means that an increase in the board size would lead to an increase in financial performance. The study also concluded that board composition and financial performance are positively and significantly related. This means that an increase in board mix would lead to an increase in financial performance.

From the results, the study also concluded that board meetings and financial performance were positively and significantly related. This means that an increase in the number of board meetings will lead to an increase in financial performance. The study further concluded that board structure and financial performance were positively and significantly related. This means that an improvement in board structure would lead to an increase in financial performance. The study demonstrated the importance of the board size on financial performance. The percentage of women in the board was found to have a significant positive relationship with financial performance. This indicates that increasing the percentage of women in the board can be associated with increase in financial performance. The study concluded that board size, board composition, Board structure and board meetings are among the main building blocks of the corporate governance mechanism.

Recommendations

The recommendations were presented based on objectives

Board size

Based on the findings and conclusion, the study recommend that though board size can have a positive effect, it does not need to increase beyond a certain limit since it can sometimes come with a disadvantage. Boards with a large number of directors can be a disadvantage and expensive for an organization to maintain. Planning, work coordination, decision-making and holding regular meetings can be difficult with a large number of board members.

Board composition

The percentage of women in the board was found to have a significant positive relationship with financial performance. Therefore this study recommends for a good representation of women in the board. Female board members usually have a better understanding of a market in comparison with male members. As such, this understanding will enhance the decisions made by the board. Second, female board members will bring better images in the perception of the community for an organization and this will contribute positively to organizations performance.

Board structure

This study shows that there is a significant relationship between board structure and financial performance. Therefore, the study recommends for a board that includes non-board members on the committees of the boards and inclusion of major donors on the board. This would make corporate governance stronger for a non-profit organization and enhance Monitoring and control of the activities of the management by the board, inclusion of donor representative in the board will help win donor confidence and trust in the organization which will result to increased funding The study further suggests a clear structure that would ensure separate roles between the board and the management.

Board meetings

This study shows that there is a significant relationship between board meetings and financial performance. The study recommends for a standard frequency of board meetings that is cost effective, the study recommend for the directors to also participate in the board meetings. They must participate in board meetings, review relevant materials, serve on board committees, and prepare for meetings and discussions with management. In addition, directors must spend the time needed and meet as frequently as necessary to properly discharge their responsibilities.

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