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EFFECTS OF CHIEF EXECUTIVE OFFICER DUALITY ON FIRM PERFORMANCE AMONG FIRMS LISTED IN NAIROBI SECURITIES EXCHANGE, KENYA

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Abstract

Finance literature suggests that CEO duality plays a critical role in determining the performance of a firm however there is a little research that has focused on the effects of CEO duality on firm performance especially on developing nations like Kenya. This study therefore sought to fill in this gap by determining the effects of CEO duality on firm's financial performance in Nairobi securities exchange. The study was guided by upper echelon theory and agency theory. The study was carried out using explanatory research design. The target population for the study comprised all listed firms at Nairobi Securities Exchange, a survey of all 45 firms that have consistently been operating at the NSE for the past 5 years from 2011-2016 was conducted. Secondary data was obtained from companies annual reports. Descriptive statistics, correlation analysis, fixed effects and Random effects regression models was adopted. Hausman test was carried out and Random effect model was found to be the best model. The study findings indicate that CEO duality had a negative significant effect on firm performance (-0.9312, p=0.000), p<0.05). The study concludes that CEO duality affects the firm performance. The study recommends firms to put in measures that ensure that the roles for the CEO and board chairman are separated to enhance the effectiveness of the board in managing the firm

Keywords: Nairobi Security Exchange, NSE, Chief Executive Officer, CEO Duality,

INTRODUCTION

Firm performance is an organization's ability to acquire and manage resources in a variety of ways in order to gain a competitive advantage. (Apiti *et al.,* (2017). Financial performance and non-financial performance are the two types of performance. Non-financial performance measures assess the firm's non-financial aspects. Non-financial performance measures include workforce development, product quality, customer satisfaction, on-time delivery, innovation, achievement of strategic goals, market share, efficiency, productivity, leadership, and employee satisfaction. (Islam *et al.,* 2015). Financial performance focuses on variables that are directly related to financial reports. Financial performance is a subjective measure of a company's ability to earn revenue from its key business assets. Financial performance measurements such as profitability and liquidity, among others, provided a significant tool for stakeholders to evaluate a firm's historical financial performance and current status.

According Terblanche *et al.,* (2013) there are three dimensions are used to assess a company's performance, dimension is the company's productivity, or the efficient conversion of inputs into outputs. The second dimension is profitability, or the extent to which a company's earnings exceed its costs. The market premium, or the amount by which a company's market value exceeds its book value, is the third dimension (Muturi & Omondi, 2013). When defining performance, two factors should be considered: the time frame and the reference point. It is feasible to distinguish between past and future performance; yet, prior superior performance does not ensure future superiority (Selvam *et al.,* 2016). Another time-related issue is the length of the interval to be considered (short, medium, or long term). The benchmark against which performance is measured, such as the industry average, key competitor results, a set goal, or previous performance (Sadeghi *et al.,* 2021), is also critical. Comparisons between targets and

previous performance reveal the company's efficiency and evolution. They are not, however, appropriate for comparing businesses of various sizes and in all industries. The baseline value of the industry or the main rivals reveals the competitive position of the company and may be more valuable for strategic assessments. In the eyes of the shareholder, a company's financial performance is measured by how much better off the shareholder is at the end of a period than he or she was at the start, and this can be determined using ratios derived from financial statements, primarily the balance sheet and income statement, or data on stock market prices (Dimitras *et al.*, 2018). These ratios can be used to compare a firm's ratios to those of other firms or to detect trends in performance over time, and they can be used to compare a firm's ratios with those of other firms. According to Fourati, & Affes, (2013) and Sethibe & Steyn, (2016), an acceptable performance metric should account for all of the effects of investments on shareholder wealth. As a result, the business's performance must be measured in terms of how much wealthy it is.

Following the recent collapse of corporate giants in the early 2000s, CEO duality, or when one person occupies both the CEO and chairman posts, has become a concerning problem. (Akisimire, *al.,* 2020; Krause *et al.,* 2014; Yang & Zhao, 2014). Surprisingly, eight of the 10 business titans implicated in corporate scandals had multiple CEOs. While this discovery has given the phrase a negative connotation, scholars are divided on how to interpret the data. Instead, the impact of CEO duality or non-duality on corporate performance has been a source of debate in academia and practice, owing to the contradicting assumptions underlying the agency and stewardship viewpoints.

The empirical research on the association between CEO duality and corporate success has been inconclusive overall (Duru *et al.,* 2016; Yang & Zhao, 2014). Dogan *et al.,* (2013), found a negative relationship between dualism and firm performance. Yu (2008), Gill and Mathur (2011), on the other hand, showed a favorable relationship between dualism and company

performance in their research. Hassanein & Wahsh, (2012); Moscu, (2013), have concluded that duality has no effect on company performance. Due to differing conclusions in the literature regarding duality and the obscurity of its effects on performance, interest in this area is expanding.

In recent years, the NSE has underperformed. The stock market's performance implies that it has not been able to make a substantial contribution to the financing of economic expansion. (Ngugi, Amanja and Maana, 2009 as cited in Maina and Sakwa, 2010). While the NSE has approximately 60 companies listed, not all of them are financially solid. Although these listed firms must meet the NSE's listing requirements at the time of listing, their financial status and business orientation can change over time for the better or for the worse. Governance, management, financial appetite, risk profile, and over gearing are just a few of the reasons for these shifts. As a result, market surveillance is required to maintain effective trade, (Maina and Sakwa, 2010). However, other publicly traded companies appear to be able to survive, therefore the question remains as to why some are functioning poorly while others fail, thereby jeopardizing investor confidence in the capital market. (CMA, 2015).

Statement of the Problem

The financial performance of businesses has drawn a lot of attention, remarks, and interest from both financial specialists, researchers, the general public, and company executives, (Manduku, (2017). Choosing the most successful companies, however, has always proven to be a challenging assignment for many, as a company might be profitable while also being in a very negative liquidity situation. The performance of the best-known listed companies in Kenya's securities market, which has over 50 listed companies, is evaluated in terms of profitability, dividend growth, sales turnover, asset base, and capital utilized, among other factors. Because a single component cannot reflect all facet of a company's performance, the integration of multiple variables provides for a more accurate assessment of a company's financial profile. The issue

then becomes determining how much weight to give to each of the factors (variables) that influence performance. (Mutula, 2018).

While some Kenyan listed companies, such as Safaricom Limited and East Africa Breweries Limited, have done well in the past, others, such as Eveready and Kenya Airways, have continued to struggle. The stock market's performance implies that it has not been able to make a substantial contribution to the financing of economic expansion (Ngugi *et al.*, 2009). While the NSE has roughly 60 companies listed, not all of them are financially sound. Although listed firms must meet the NSE's listing requirements at the time of listing, their financial status can change for the better or for the worse over time. This fluctuation in profit implies that certain specific circumstances have a significant impact on a company's profitability. As a result, it is critical to determine the impact of CEO duality and how it relates to business profitability in Kenya.

Few studies have been done on Pham & Pham, (2020) assed the impact of CEO duality on firm performance. According to the research, CEO duality has a beneficial impact on firm performance. Duru*et al.,* (2016), investigated the dynamic relationship between CEO duality and firm performance. The results indicated that CEO duality has statistically significant negative impacts on firm performance. Yasser *et al.,* (2015), examined the relationship between CEO duality and the performance of Pakistani public listed companies. The results suggested that CEO duality is a less significant issue in corporate governance.Despite previous studies on CEO duality and business performance, the impacts of CEO duality are unclear in firms listed on the NSE, and studies conducted have been ambiguous, necessitating the conduct of a study on the relationship between CEO duality and firm performance. This research sought to establish whether CEO duality has an effect on firm’s financial performance of firms listed in NSE.

LITERATURE REVIEW

Concept of CEO Duality

The term "duality" refers to a corporate leadership structure in which one person serves as both CEO and Chairman of the Board of Directors. (Krause *et al.,* 2014; Wang *et al.,* 2014; Terinte, (2019), CEO Duality and Firm Profitability as evidence from Emerging Europe has become an emerging issue of research in the current era following corporate scandals around the world (Gove & Junkunc, (2013). The terminology 'CEO duality' in the literature is diverse. The dual position (CEO and chairman is the same individual) is also referred to as combined CEO/Chairman (Krause *et al.,* 2014), CEO-chair duality (Rutledge *et al.,* 2016), unitary leadership structure (Guillet, *et al.,* 2013), joint CEO/chairman (Moscu, 2013), and CEO as chairman, among others.

The different arguments in favor of duality all agree that merging the CEO and Chairman positions improves the functioning of the board. The stewardship hypothesis, according to Arslan *et al.,* (2014), provides a complementary perspective by claiming that agents are good stewards of an organization's resources. Stewardship theorists argue that there is no inherent conflict of interest between agents and principals because, among other things, CEOs will not jeopardize their image and careers by pursuing interests that are incompatible with the interests of shareholders..

Duality proponents further believe that a combined role gives a combined command structure, a single focal point, and lowers the company's decision-making costs. A CEO-Chair might have more authority and speed in making and implementing strategic choices for the company, giving it a more stable appearance. As a result, choices made by a CEO-Chair on a major topic may be clearer, faster, more consistent, and more timely than judgments made by a CEO who must negotiate and confer with a board led by a different Chair. Furthermore, having only one person

serve as both CEO and Chair avoids public uncertainty about who is in command of the organization and explains who is responsible for its success and long-term viability. According to agency theorists, the separation of the CEO and Chairman's positions (Khan *et al.,* 2013) protects accountability but hindering the board's ability to supervise management opportunism because the CEO has a tendency to manipulate the board (Wang *et al.,* 2014). Supporters of the agency theory believed that separating the board's management tasks improves the board's performance by boosting the superiority and suitability of decision-making.

A nonexecutive board Chairperson can provide fresh information, self-determination, and insights to the board's process, as well as unique perspectives that improve the board's ability to deliberate and make strategic and essential business decisions in its management obligations. According to Yasser, & Al Mamun, (2015), the lack of desire and incentive to objectively evaluate and discipline the dual executive reduces the risk of entrenchment, which increases the risk of the CEO-Chair in both roles.The entrenchment of multiple positions, on the other hand, enhances the potential for this powerful CEO to use the firm to serve his own private interests rather than the general good of shareholders.

When the chairman of the board is also the CEO of the firm, all of the corporation's powers are concentrated in one person, and the chance of CEO authority being checked and balanced is essentially removed. The board of directors of such a corporation may not be able to function as an independent body, even though it is the board's aim. According to the agency hypothesis, separating the roles of CEO and chairman will reduce the opportunity for the CEO and inside directors to engage in self-motivated and financially costly actions. Nishanthan, *et al.,* (2014) recommended the separation of CEO and board chairman jobs; one person cannot effectively fulfill both roles because they each have their own domain.

Concept of Firm Performance

Firm performance is defined as a monetary measurement of the outcomes of a company's policies and operations. These outcomes are indicated by the company's gains from new ventures, used resources, increase in value, among others .According to Verreynne and Meyer (2008), scholars and government agencies alike are concerned about the relative productivity of different enterprises. The hunt for characteristics that may offer firms with competitiveness and so boost firm profitability is the driving force behind this type of research. Despite the importance of the construct and the attention it has received, defining and assessing performance for a specific industry has always been a research topic in recent years.

Performance varies as much between different competitive contexts as it does between different businesses. As a result, investigating single firms rather than the industry as the primary unit of analysis might assist scholars in gaining a more in-depth understanding of firm rivalry patterns and performance factors (Houthoofd, & Hendrickx, 2012). Firm performance refers to a company's actual output or results as compared to its intended outputs (or goals and objectives). Business productivity, according to Richard *et al.,* (2009), encompasses three distinct dimensions of a company's output: (a) financial output (profits, return on assets, and return on investment); (b) product market output (sales, market share); and (c) shareholder return (total shareholder return, economic value added). Specialists in many fields are concerned with structural productivity, including strategic planners, operations, finance, legal, and structural development.

Different firms use different methodologies to measure their performance depending on their structural goals. This metric can be determined using both monetary and non-monetary criteria (Bakar & Ahmad, 2010). Despite this, the majority of organizations choose monetary productivity indicators (Mohamad & Sidek, 2013). Return on assets (ROA) (Zahra, 2008), average annual occupancy rate, net profit after tax and return on investment (ROI)

(Tavitiyaman*et al.*, 2012) are the commonly used financial or accounting indicators by firms. Other popular indicators of performance include internal efficiency, development, shareholder fulfillment, marketplace stake and competitiveness (Bagorogoza& Waal, 2010). Money functions, on the other hand, are not the only indicators of productivity. In this study, it combines both financial and non-financial measurement in order to adapt to the changes of internal and external environments (Njeri, 2017).

Relationship between CEO duality and firm Performance.

Various authors have found different results on the relationship between CEO duality and firm performance. Pham & Pham, (2020). The impact of CEO duality on firm performance. The data is balanced and covers over the period 2012–2018 for 442 publicly listed firms in Vietnam. The findings indicated that CEO duality had a positive effect on firm performance in growth stage and had a negative effect on the mature stage of the firm's life-cycle. These results are supported by stewardship theory which argues that CEO duality may be good for firm performance in the growth stage due to the unity of presented command. In contrast, agency theory shows CEO duality is bad for firm performance in the maturing stage since it compromises the monitoring and controls the behavior of the CEO. Also, this study shows that there was a difference between state shareholders and director from outside of the company affecting the firm performance.

Duru *et al.,* (2016), the dynamic relationship between CEO duality and firm performance. The results indicated that CEO duality has statistically significant negative impacts on firm performance. Nazar, (2016), examined the impact of CEO duality on firm performance of listed non-financial firms in Sri Lanka. This study uses the ROA as proxy measure for form performance. This study employed a cross sectional ordinary least square analysis of 128 firms listed in Colombo Stock Exchange (CSE) for the financial year ending 2013. The results show that CEO duality is significantly negatively associated with ROA.

Yasser *et al.,* (2015), examined the relationship between CEO duality and the performance of

Pakistani public listed companies by using a sample of five years, from 2007 to 2011. The study tested the hypotheses with data obtained from the Karachi Stock Exchange 100 indexed firms, and employed the agency and stewardship theory perspectives. The results suggested that CEO duality is a less significant issue in corporate governance than suggested by many previous researchers and policy makers.

There is a significant relationship between CEO duality and firm performance.

RESEARCH METHODOLOGY

This study used explanatory research design. The study targeted 67 firms listed on the NairobiSecurities Exchange the study sampled all firms that had been listed on the Nairobi SecurityExchange (NSE) during the 5 year study a sample of 45 firms was arrived at purposively aftereliminating the number of firms delisted, suspended, terminated and those with missing data.The study got its data from secondary sources data was collected from the annual reports offirms listed on the Nairobi Security Exchange (NSE) from 2011 to 2016. The researcherselected 2011 to 2016 because during these 5 years the selected firms had been consistentlytrading in N.S.E.

The study conducted initial data analysis using descriptive statistics, correlation analysisand the fixed effects and random effects regression models. The descriptive statistics of thefirms provides an overview of the background analysis of the sample used in this study as wellas results on study variables. The regression model for the fixed and random effects wererespectively stored and there after a Hausman test was carried out to establish the best modelin predicting the changes infirm performance.

$Yit = \alpha it + \beta 1it + X1it + \varepsilon it$

Y = the dependent variable (Firm Performance)

α = Constant

ε = Error term

β1= is the regression coefficient in Y by each X variable.

X1= CEO duality

t = measure of time

i = number of firm observation

The above statistical tests were analyzed using Stata 13. All tests were two-tailed. Significant levels were measured at 95% confidence level with significant differences recorded at $p < 0.05$.

RESULTS

Descriptive Analysis

Table 1. Descriptive Statistics

Variable		Mean	Std. Dev.
EPS	Overall	1.376726	3.41748
	Within		3.18797
CEO duality	Overall	0.33489	0.29057
	Within		0.14528

The findings in Table 1. EPS, representing the measure of firm performance has a mean of 1.377 with an overall standard deviation of 3.417 and a within standard deviation of 3.188. CEO duality has a mean of 0.33489with an overall standard deviation 0.291 and a within standard deviation of 0.145.

Correlation Analysis

Correlation analysis is usually carried to determine the degree to which two variables converge or diverge together depending on the case so as to establish the significance of the relationship. As such, a positive value of the correlation coefficient shows that the two variables move together in the same trend, and when there is a negative value, it shows that the variables move

in opposite direction or trend. Essentially, correlation analysis depicts to a given degree, the aspect of how one factor influences another although correlations do not imply a cause-effect relationship. Consequently, a correlation analysis of the independent factors and the dependent factor was carried out and the findings were summarized and presented in Table 2.

Correlation Analysis

Table 2. Correlation Analysis

	EPS	CEO duality
EPS	1	
CEO duality	0.2676*	1

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

The findings in Table 2 revealed thatCEO duality has a positive and significant relationship with firm performance (EPS), 0.2676 meaning that there is 26.76% chance that firm performance will increase with increase in CEO duality

Fixed Effects Model

Fixed-Effects GLS Regression

Table 3 Fixed Effects regression model of CEO duality on firm performance

			Number of obs = 225			
Group variable: firm			Number of groups = 7			
R-sq: within = 0.371			Obs per group: min = 8			
between = 0.3310			avg = 10.1			
overall = 0.3784			max = 11			
			Wald chi2(6) = 313.6			
corr(u_i, X) = 0 (assumed)			Prob> chi2 = 0.000			
Firm performance	**Coef.**	**Std. Err.**	**T**	**P>t**	**[95% Conf. Interval]**	
Control variables						
CEO duality	-0.175	0.014	12.27	0.000	-0.147	-0.203
_cons	-12.789	2.014	-6.35	0.000	-16.737	-8.842
sigma_u	1.956					
sigma_e	3.263					
rho (fraction of variance due	0.157					

to u_i)

Dependent Variable: Firm Performance (EPS)

The results presented in Table 3 revealed that the overall model while controlling for firm size and firm age was found to be significant, with at least one estimated coefficient found to be different from 0,Wald chi2(6) = 313.6, p-value = 0.000. The findings showed that the estimated standard deviation of α_i (sigma_u) is 1.956 which is greater than the standard deviation of ε_{it} (sigma_e) = 3.263 suggesting that the individual-specific component of the error is more important than the idiosyncratic error. Furthermore, assessing the t-values revealed that the t-value for C.E.O duality, was greater than +/-1.96 (at 95% confidence) and this implied that firm size,C.E.O duality was different from 0. The findings showed that C.E.O duality (-0.175, p = 0.000), had significant effect on firm performance. In addition, this means that with each unit increase in C.E.O duality, there is -0.175 unit decreases in thefirm performance

In addition from the findings, 15.7 % of the variance is due to differences across panels; 'rho' is known as the intra-class correlation.

Random Effects models

Table 4. Random Effects regression model of CEO duality on firm performance

R Square within	0.371			**Number of obs = 225**		
Wald Chi square	2.75			Number of groups = 7		
Prob> Chi square	0.0201			Obs per group: min = 8		
corr(u_i, X) = 0 (assumed)						
	Coef.	Std. Err.	T	P>Z	[95% Conf. Interval]	
predictors						
CEO duality	-0.9312	-0.0759	12.27	0.000	0.147	0.203
_cons	-12.789	2.014	-6.35	0.000	-16.737	-8.842
sigma_u	1.27083					
sigma_e	3.421					
Rho	0.121283					

Dependent Variable: Firm Performance (EPS)

The findings in Table 4 revealed that the overall model while controlling for firm age and firm size was found to be significant, with at least one estimated coefficient found to be different from 0, Wald χ^2 2.75 = 2.75, p-value = 0.0201 showing that the variation of EPS was dependent on the model. The findings showed that the estimated standard deviation of α_i (sigma-u) is 1.27083 which is smaller than the standard deviation of ε_{it} (sigma-e) which is 3.421suggesting that the individual-specific component of the error is less important than the idiosyncratic error. Furthermore, assessing the t-values revealed that the t-values C.E.O duality, was greater than +/- 1.96 (at 95% confidence).

The findings showed that CEO duality (-0.9312, p=0.000) has significant effects on the firm performance. This implies that with each unit increase CEO duality, there is -0.9312 unit decreases in firm performance. In addition from the findings, 12.1% of the variance is due to differences across panels; 'rho' is known as the intra-class correlation.

Hausman Test

Table 5. Selecting between Fixed Effect Model and Random Effects Model

	---- Coefficients ----			
	(b) Fixed	**(B) random**	**(b-B) Difference**	**sqrt(diag(V_b-V_B)) S.E.**
CEO duality	-0.2555767	-0.6484513	0.3928746	0.3497586
interaction	0.0569217	0.0699023	-0.0129806	0.0135702

b = consistent under Ho and Ha; obtained from xtreg

B = inconsistent under Ha, efficient under Ho; obtained from xtreg

Test: Ho: difference in coefficients not systematic

chi2(5) = (b-B)'[(V_b-V_B)^(-1)](b-B) = 4.15

Prob>chi2 = 0.5284

From the findings in Table 5, the chi2 statistic was 4.15 which was not significant, p-value =0.5284 indicating that the test is in favor of the random effects model which had reducedstandard errors compared to the fixed effects model. This means that the most appropriatemodel that can effectively explain firm performance (EPS) is the random effects model.

Hypothesis Testing

Hypothesis 1(Ho1) revealed that there was a significant effect of CEO duality on firm performance. Findings show that CEO duality had coefficients of estimate which was significant basing on (-0.9312, p=0.000), p<0.05). This implies that with each unit increase CEO duality, there is -0.9312 unit decreases in firm performance, implying that we accept the hypothesis and infer that CEO duality has a negative significant effect on firm performance.

CONCLUSION

The primary objective of this study was to examine effects of CEO duality on firm performance in Nairobi stock exchange. On the effect of CEO duality on firm performance, the firm has showed that CEO duality has a negative effect on firm performance. While there are supporters of CEO duality, agency theorists have pointed out that the separation between the roles of the CEO and Chairman safeguards accountability and impair the board's ability to monitor managerial resourcefulness because CEO has the propensity to control the board and will decrease the opportunity for the CEO and inside directors to exercise behaviors which are self-motivated and costly to the provision of finance (Principal). In addition, the separation of the roles enhances the board's effectiveness in management responsibilities by improving both the superiority and the suitability of decision making.

RECOMMENDATIONS

CEO duality has a significant effect on firm performance, there is need to harness the positives of CEO duality such as the increase in the level of effectiveness. This can be done while at the

same time ensuring that the dual role does not negatively impact on the growth of the firm. In addition, the operational policy of the firm is important in ensuring that there is no conflict of interest between the functions of the CEO and the chairman being vested in one individual. In addition, an effective operational policy of the firm will ensure that the dual role assumes an effective command structure while reducing the firm's cost in decision making. If this is not the case, there is need for the firms to put in measures that ensure that the roles are separated to enhance the effectiveness of the board.

RECOMMENDATIONS FOR FURTHER RESEARCH

The study primary focus of this study was to establish the effect of CEO duality on firm performance among listed firms in NSE. The findings have pointed to the existence of a negative relationship between CEO duality and firm performance Thus, there is need to carry out further research while also including such time- invariant variables and partial time invariant variables. In addition, there is need to pool in more firms that are listed on the stock exchange in order to enrich the data while providing an even firmer platform for regulators and policy makers to develop even more sound policies and frameworks that would guide the growth of the firm and safeguard the shareholders against loses.

Furthermore, the data utilized in this research was secondary data obtained from the Nairobi Securities Exchange. Thus, more research can be carried out by utilizing a research design that would enable collection and utilization of primary data from the firms thereby developing a confirmatory mechanism to the findings of this study.

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