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Board independence, CEO tenure, and private firm performance in Nairobi, Kenya

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Abstract

Governing board members includes a mix of non-executive and executive members who seek the best interests of shareholders. Non-executive board members relay on independence to execute their responsibilities and enables better firms' performance. The independent board members are vetted in by shareholders to reduce agency problems. The study aims to establish how Chief executive officer tenure influence independent board members on decision making to enhance firm performance. Agency theory and stewardship theory were utilized in the study. The explanatory research design was used 371 private firms were the sample size. Data was collected using structured questionnaires. Hierarchical multiple regression models were used to test for direct effect and moderation effect. According to the findings, board member independence is critical for monitoring the CEO and reducing principal-agent conflict, hence enhancing business performance. The independence of board members is critical for organizations to remain inventive and competitive in order to improve firm performance.

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1. Introduction

Despite the bankruptcy of multiple significant firms, including WorldCom and, Enron the majority of businesses have recognized the vital roles played by members of the board who are independent. The key role of the board is to define the firm's strategies as well as ensure efficient oversight of the business's operations (Vitolla, Raimo, & Rubino, 2020). Independent board members offers unique viewpoints as well as take part in the board's meetings. Board members are going to be on the company's board as they represent shareholders. Independent board members guarantee that the firm's choices are untainted by internal or managerial influence. The business appoints independent directors to regulate the work of the CEO visa-a-visa performance. Precisely the board, will prioritize the interests of shareholders by generating more value for them. As noted by Zinkin (2010), board independence ought to consider a variety of variables which contributes towards the successful implementation regarding the company's overall strategies. The firm's operations, its product market differentiation, as well as important customers beneath the market should be investigated by an independent board (Olie, Klijn, & Leenders, 2020). Independent board members with extensive industry expertise and experience may likely to critique CEOs and executive teams in boardroom discussions.

Neifar, Salhi, and Jarboui (2020) explored board members independence being a critical part of ensuring the efficiency of boards via surveillance as well as managerial responsibilities. Having an appropriate number of board independence in the firm is the most important part of ensuring board effectiveness. Board members who are independent with diverse skill/expertise, eagerness, and member atmosphere of the boards' increases member's independence (Minichilli, Zattoni, & Zona, 2009). In the findings of Fuzi, Halim, and Julizaerma (2016), the formal independence, accessibility of knowledge, incentives granted, and competence of independent board members in China impact the way firm attain its performance. They eventually found that China's independent board system in place is insufficient as a result of excess involvement from shareholders with power as well as dearth of knowledge of independent boards' functions.

McCabe and Nowak (2008) interviewed 30 directors to investigate the functions of independent directors in Australian publicly traded firms. The findings indicate that a large proportion of independent board members, concurred that their actions were going to safeguard the separation of power and CEO. There was also a distinction among independent and non-independent board members. Furthermore, the presence of independent board members could offer numerous types of critical thinking, and virtually board members are able to reduce the hazards of "collective thinking.' The study extends the focus of CEOs influences on board decision due to lack of independence. According to Bliss (2011), found that there's no correlation between independent board members and CEO's duality and firms' overall performance. Duru, Iyengar, and Zampelli (2016), on the other hand, conclude that an adverse association involving CEO duality and independence from the board.

In their study on board member's independence in licensed companies in Turkey, Ararat, Orbay, and Yurtoglu (2010) revealed some main important findings. Initial results suggested that independent board members and equity holders were not having meaningful impact on the firm. Furthermore, they also identified an adverse relationship and a non-relationship between board independence and company outcomes. These findings were caused by the notion that Turkish registered companies' board members we're not truly independent. A number of the unbiased board members possessed professional, monetary, and social links to the major investors, which interfered with board opinions and hacked their capacity to function as independent boards.

2. Literature Review

2.1. Concept of Board Independence

The term "independence of a board member" refers to a situation in which a board member has no direct or indirect substantial relationship with the firm, its affiliates, or any of its members other than a member of the firm's board (Corbetta & Salvato, 2004). The success of board members in their positions is dependent on their independence. Members of independent boards are more adept at oversight and overseeing firm performance (Terjesen, Couto, & Francisco, 2016). Furthermore, Ramón-Llorens, García-Meca, and Pucheta-Martínez (2019) discovered that independent directors are motivated to watch management via their desire to develop a track record as experienced monitors and competent individuals. Additionally, there is a considerable corpus of research on the association between independent boards and corporate outcomes (Fuzi et al., 2016; Guerrero, Lapalme, Herrbach, & Séguin, 2017).

2.2. Concept of CEO Tenure

CEO tenure signifies the amount of period an individual serves as CEO, and it is an important factor in the current contemporary CEO study (Finkelstein, Hambrick, & Cannella, 2009; Hambrick & Fukutomi, 1991). Hambrick and Mason (1984) cited "CEO tenure" as a crucial visible factor that reflects the same "inherent & actions" by CEOs over their term in office in their landmark work. CEOs take actions that influence the destiny and fates of their businesses while in office (Hambrick & Fukutomi, 1991; Miller, 1991). Grasp the functions and actions of CEOs in general requires a thorough grasp of CEO tenure.

2.3. Relationship between Board Independence and Firm Performance

Board independence is a word that refers to independent board members, non-independent board members, and outside directors. Research on board members' independence and business performance yielded inconsistent results, with either a favorable, negative, or no relationship with the performance of the firm. There has been limited study into the association involving independent board members and managing earnings. Market-based or accounting-based measures have been used in studies on firm performance. Accounting-based metrics include earnings per share, Return on Assets, Return on Investment, and profit. In contrast, several research use Tobin's q for market value as a market-based indicator.

A study conducted in India discovered that maintaining members of the board who are independence does not guarantee increased performance of the firm because of independent boards' inadequate oversight responsibilities (Mishra, 2023). One of the most significant roles of independent board members is to monitor the business's finances and operations. An effective oversight approach inside the organization may aid in the reduction of agency concerns. The study also suggests that the corporation appoint independent board members capable of providing adequate oversight in the fields of governing, control systems, and risk mitigation.

Other corporate governance mechanisms, such as board member independence and committee on auditing, are associated with a minimal relationship with earnings management in Malaysian firms reducing firm performance, according to Abdul Rahman and Haneem Mohamed Ali (2006). One possible cause as discussed is the failure of board members, as well as poor monitoring tasks as a result of management and CEOs domination in board matters. A comparable study on board member committee independence and business performance in Hong Kong family-owned companies revealed no association on the relationship (Leung, Richardson, & Jaggi, 2014). However, evidence suggests a positive relationship between board member independence and firm success in nonfamily enterprises (Liu, Mihail, Miletkov, Zuobao, & Tina, 2015; Potharla & Amirishetty, 2021). Precisely retaining independent board members on the board is essential because it leads to improved business outcomes.

Fauzi and Locke (2012) discovered a considerable negative association between the percentage of non-executive board members and company performance in a study of businesses registered on the New Zealand Stock Exchange from 2007 to 2011. This implies that the greater the number of independent board members on the board, the poorer the firm. This adverse connotation could be attributed to the large percentage of block holders, making independent board members ineffective in board deliberations. Independent board members on the board can guarantee that top leadership uses the firm's assets in as effective a way as is feasible to generate profitability.

According to a research of Pakistani boards, the percentage of foreign boards has an adverse correlation with corporate success. This is due to the fact that, small number of outside board members on the board mean low board independence (Ahmed Sheikh, Wang, & Khan, 2013). Board independence guaranteed that the corporations practiced effective corporate governance. Also, Foo and Zain (2010) studied the board member independence, board diligence, and liquidity of 481 Malaysian public-listed businesses at the end of 2007. According to the findings, when board members are independent, they are more honest and share details that enhances the company's financial stability and productivity.

H_{01}: Board independence increases firm performance.

2.4. Theoretical Review

Previous research on the relationship between independent board members and business performance has been inconsistent. Studies back up the agency theory research papers by finding a positive relationship between independent board members and firm outcomes (Liu et al., 2015; Rashid, 2018; Uribe-Bohorquez, Martínez-Ferrero, & García-Sánchez, 2018). Other studies, on the other hand, support the stewardship theory concept and show a negative relationship between independent board members and corporate outcomes (Bhagat & Black, 2001; Cavaco, Challe, Crifo, Rebérioux, & Roudaut, 2016; Pathan, Skully, & Wickramanayake, 2007). Rather than the stewardship hypothesis, the agency theory might address the inconclusive data on independent board members and business outcomes (Samara & Berbegal-Mirabent, 2018; Shan, 2019). The assumptions of agency theory, according to Shan (2013), explain that top executives have motives and that independent board members operate as a dependable oversight system to safeguard shareholders, constrain directors' selfish motivated actions, and mediate the principal-agent tension. Since a larger number of independent board members can successfully carry out oversight functions and support improved firm performance (Fama & Jensen, 1983; Jensen & Meckling, 2019).

In line with the stewardship theory, CEOs are dependable people and ethical protectors who respond on behalf of shareholders, and that board members should be controlled by internal or dependent board members because they strive to maximize shareholder value and have more accurate knowledge and expertise that facilitate efficient decisions than independent board members (Davis & Greve, 1997; Donaldson & Davis, 1991). Both of these hypotheses, according to Ghosh and Harjoto (2011), may be compatible but are not necessarily contradictory. Under certain conditions, an inside board member may choose to be an agent or a steward. Using multi-stage simultaneous equations, previous study addressed the possibility of endogeneity and developed an asymmetrical correlation relating independent board members and business outcomes. Young, Peng, Ahlstrom, Bruton, and Jiang (2008) for example, to address the issue of endogeneity between board member independence and corporate profitability, researchers used a concurrent equation with the percentage of independent board members as a dependent variable. After adjusting for endogeneity, they discovered two-way causation and observed positive associations between the proportion of independent board members and business outcome. Setia-Atmaja (2009) also looked into endogeneity.

2.5. The Link between CEO Tenure Firm Performances

Long-tenured CEOs might get anchored for a number of reasons, according to agency theorists (Shen, 2003). Firstly, CEO power may expand with tenure as a consequence of an excellent history of achievement. Secondly, long-term CEOs may have an influence on board structure. The long-tenured CEO might have greater influence over the election of upcoming members of the board, leading to a board that is devoted and empathetic to the CEO. Lastly, when they gain control over procedures and internal information systems, CEOs may grow their relative authority. Control over information processes and systems may allow CEOs to suppress vital information or manipulate the board discussion.

The stress placed on new CEOs is likely to be greater than on older CEOs because they have yet to establish their ability to succeed in their new roles. In order to secure their new jobs, new CEOs will strive to build early records of success (Harrison & Fiet, 1999). Thus New CEOs are easily monitored by independent board members, this increases firm performance (Bhagat & Black, 1999; Bommaraju, Ahearne, Krause, & Tirunillai, 2019). Also new CEOs may facilitate new projects in the firm and end up reducing firm performance. Long-tenured CEOs may have significant power over board member selection and cultivate personal relationships with board members (Walters, Kroll, & Wright, 2007). Eventually, such board members may learn to blindly trust their CEOs (Gentry, Harrison, Quigley, & Boivie, 2021; Guldiken, Mallon, Fainshmidt, Judge, & Clark, 2019). As a consequence of such a power shift, CEOs may pursue personal gains other than shareholder interests, such as firm expansion, in order to justify higher monetary benefits (Davis, 2019), risk diversification (Wang & Chen, 2020), and the satiation of their own narcissism as such CEOs may not focus on firm performance thus reducing (Zhu & Chen, 2015). When CEOs' tenure goes from low to large levels, their task knowledge plateaus, and they gain authority vis-à-vis the board, aiding corporate outcome (Zorn, DeGhetto, Ketchen Jr, & Combs, 2020).

Since the critical nature of CEO tenure and the amount of literature in the two studies categories are compelling grounds to analyze the existing information, this kind of review also contributes to CEO studies in broad. The fundamental position element that represents the effect of time on a CEO is CEO tenure (Hambrick & Fukutomi, 1991; Miller, 1991). Consequently, studying CEO tenure will offer a smooth knowledge of when and how CEOs affect board members decisions in the boardroom and firm outcomes (Bertrand, 2009). This study fill in the gap on either long tenured CEOs or new CEOs influence independent board members on the decision regarding firm performance. The relationship are presented in Figure 1.

2.6. Conceptual Framework

The conceptual framework shows the association on the direct effect and indirect effect that is, how board member's independence influences firm performance and how CEO tenure moderates the relationship between board members independence and firm performance. The study control variables were the size of the board, gender of the CEO and the size of the firm, this may affect the outcome of the study.

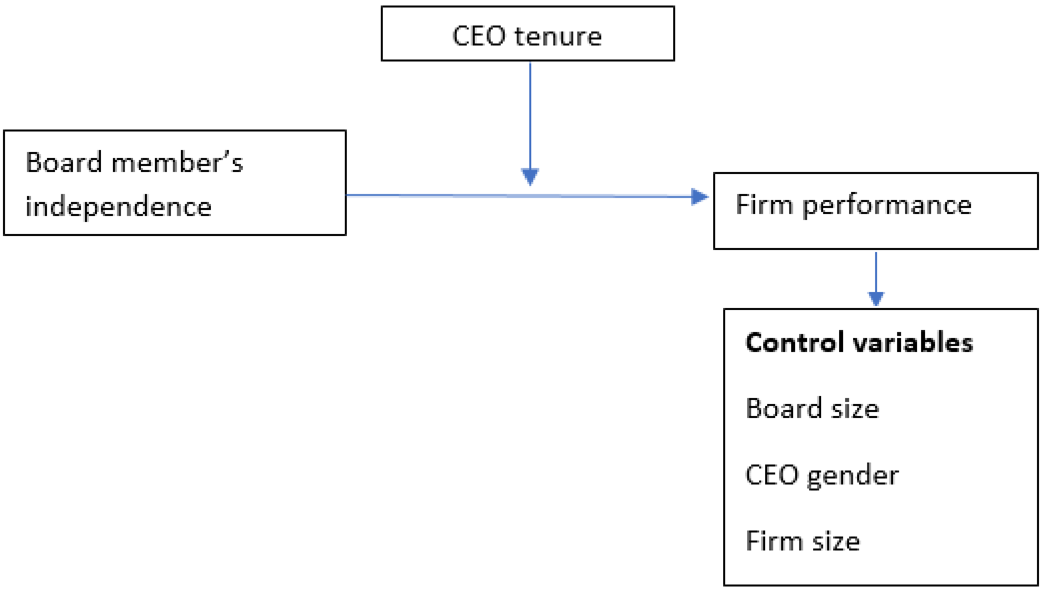

Figure 1. Conceptual framework.

3. Methodology

This study made use of explanatory research. It seeks to establish the causal connection among the variables being studied via acknowledging the way one component affects the other; it seeks to provide exploratory explanation to the cause-and-effect situation, and final outcomes interaction among one or more variables (Hair Jr, Matthews, Matthews, & Sarstedt, 2017). Modules are also used when the purpose of the study is to clarify the "why" in each situation. As stated by Blumberg, Cooper, and Schindler (2014), exploratory study targets why questions. The study was concerned in formulating and offering clarifications to the 'why' questions. The clarifications contend that a phenomenon Y (firm performance) is influenced by factor X (board independence and CEO tenure). This was used on the grounds that it connected nearly to the goals of this study and was functional in testing the results of the study.

The study target sample was 402 private firms in Nairobi county Kenya. The study used primary data since it suites the nature of my study to obtain first-hand information and to obtain the required output. Primary data was appropriate because private sector is not required by law to publish their books of account making them unreliable for secondary data. The use of primary data has been lauded as an alternate method of verifying governance theories that are primarily dependent on secondary data. The questionnaires generated from earlier research were utilized to gather information from a selected number of 402 accessible enterprises. In the analysis, 371 valid questionnaires were employed.

Researcher used a hierarchical regression analysis to assess our assumptions, as described by Aiken and West (1991). We used Variance Inflation Factors (VIF) to test the variables for multicollinearity before running the regression analysis. VIF values for every variable were within the standard threshold of 10 (Hair, Sarstedt, Ringle, & Mena, 2012) indicating that there was no problem with multicolllinearity. Researcher also used residual plots to evaluate for data normality and plotted a graph. Data was normal distribution. We normalized all independent variables before running the regression analysis to reduce the multicollinearity problem that occurs when a moderator variable is estimated as the product of two variables, namely a moderator and an independent variable (Aiken & West, 1991). All of the independent and moderated variables were included into the regression equation at the same time to evaluate the moderated regressions.

3.1. Modelling Specification

The collected data was analysed using multiple regression model and hierarchical regression models and the significant of independent variable was tested at a confidence level of 95%. The multiple regression equation will be shown as follows:

$$FP = \alpha + C + \varepsilon \quad (1)$$

Where FP represent firm performance, α represent a constant C represent all control variables and ε represent the error term. Equation 1 present the coefficient of all control variables on firm performance.

3.1.1. Hierarchical Model

$$FP = \alpha + C + \beta_1 BI + \varepsilon \quad (2)$$

$$FP = \alpha + C + \beta_1 BI + CT + \varepsilon \quad (3)$$

$$FP = \alpha + C + \beta_1 BI + CT + BI * CT + \varepsilon \quad (4)$$

Where FP represent firm performance, α represent a constant C represent all control variables, β_1 present coefficient of independent variable, BI represent board member's independence and ε represent the error term. Equation 2 explains the coefficient of interaction terms of board member's independent variable on firm performance and control variables.

Equation 3 explains the coefficient of all control variables, board independence and CEO tenure as a moderator. Equation 4 explain the coefficient of all control variables, board member's independence, CEO tenure and the interaction of CEO tenure and board member's independence.

4. Analysis and Presentation of Data

4.1. Descriptive Statistics on CEO Tenure

From the findings in Table 1 indicate that out of 371 CEO respondent, majority had been CEO for a period of 2-5 years with 47.7% while above 10 years of being CEO were 8.6%.

Table 1. CEO tenure.

CEO age bracket		Frequency	Percent	Valid percent	Cumulative percent
	Below 2 years	38	10.2	10.2	10.2
	2-5 years	178	47.7	48.0	58.2
	6-10 years	123	33.0	33.2	91.4
	Above 10 years	32	8.6	8.6	100.0
	Total	371	99.5	100.0	100

4.2. Descriptive Statistics on Board Member's Independence

Board member's independence was measured using six constructs. The response was categorized into five Likert scale as 5=strongly agree, 4 = agree, 3 = neutral, 2 = disagree and 1= strongly disagree.

Table 2. Descriptive statistics on independent board members.

Measurement item of board independence	Mean	Std. deviation	Skewness	Kurtosis
Our board members have no close friendship connections to the CEO.	4.05	1.201	-1.246	0.511
Our board members have close business ties to the firm.	4.20	1.112	-1.354	0.941
Our board members have no close family relations to the CEO.	4.11	1.137	-1.150	0.213
Our board members have no close connections to each other through common membership on other boards.	4.18	1.131	-1.109	-0.195
Our board members have close ties to other persons and firms which holds large stakes in the firm.	4.20	1.101	-1.158	0.051
Our board members are free to object or disapprove CEOs decisions or suggestions.	4.21	1.157	-1.191	-0.026
Valid N	371	**371**	**371**	**371**

Form Table 2 majority of the respondent agreed on the statements regarding board member's independence and that board members are free to disapprove CEO decisions. The data were negatively skewed and kurtosis was flatter but not far from a normal distribution curve.

4.3. Descriptive Statistics on Firm Performance

Firm performance was measured using eleven constructs. The response was categorized into five Likert scale as 5=strongly agree, 4 = agree, 3 = neutral, 2 = disagree and 1= strongly disagree.

Table 3. Descriptive statistics on firm performance.

Measurement items of firm performance	Mean	Std. deviation	Skewness	Kurtosis
FP1 In the last three years, our company has been extremely prosperous.	4.32	0.856	-1.324	1.962
FP2 In the last three years, our company has earned a huge volume of sales.	4.15	1.146	-1.511	1.437
FP3 In the previous three years, our company has grown rapidly.	4.12	1.043	-1.142	0.672
FP4 In the last three years, our company's profitability has increased.	3.91	1.247	-0.845	-0.533
FP5 In the last three years, our company has improved its strategic position.	4.01	1.154	-1.118	0.369
FP6 In the last three years, our company has dramatically increased the size of its market.	3.77	1.224	-1.072	0.232
Valid N	371	371	371	371

Table 3 present descriptive statistics of firm performance and it reveal that majority of the respondent agreed that there firm had been profitable for the last three years. The data were negatively skewed while kurtosis was flatter but not far from a normal distribution curve, hence the data was normally distributed.

4.4. Multi-Collinearity Statistics

Table 4 present the collinearity statistics that is correlation between predictor variable and morerating variable (or independent variable), such that they express a linear relationship in a regression model. When predictor variables in the same regression model are correlated, they cannot independently predict the value of the dependent variable. The assumption of multicollinearity was not violated and that there was no multicollinearity since tolerance was above 0.2 and variance inflation factor less that 10 implying no/minimal multicollinearity (Alin, 2010).

Table 4. Collinearity statistics.

Variables	Tolerance	VIF
CEO gender	0.916	1.092
Board size	0.131	7.612
Firm size	0.137	7.322
Board independence	0.984	1.017
CEO tenure	0.943	1.346

4.5. Correlation Analysis

Table 5 present correlation analysis that is a change in board member's independent corresponds to a change in firm performance so as to CEO tenure. The findings indicate that CEO gender negatively correlate to firm performance while board member's independence positively correlate to firm performance, this suggest that independent board members enhances firm to increase its performance. Also CEO tenure negatively correlate to firm performance. This implies that when CEO tenure is increased it reduces firm performance.

Table 5. Correlations analysis.

Variables	Firm performance	CEO gender	Board size	Firm size	Board independence	CEO tenure
Firm performance	1.000					
CEO gender	-0.144**	1.000				
Board size	-0.047	0.211	1.000			
Firm size	0.009	0.164	0.755	1.000		
Board independence	0.311***	-0.022	0.026	0.067	1.000	
CEO tenure	-0.133**	0.074	0.010	0.010	-0.058	1.000

Note: **. Means that the Correlation is significant at 5 % level.
***. Means that Correlation is significant at 1 % level.

4.6. Regression Analysis and Hypothesis Testing

Table 6 represent regression for all control variables, independent variable and moderating variable on dependent variable. The findings indicates that in Model 1 control variable CEO gender is negatively significant to firm performance implying that when CEO gender is considered in an organization it is likely to reduce firm performance. In Model 2 CEO gender is Negatively significant while board member's independence is positive and significant to firm performance, this imply that increase in board member's independence increases firm performance. Model 3 indicate that CEO gender is negatively significant to firm performance. Board member's independence is also positive and significant to firm performance, while CEO tenure is negatively significant to firm performance this can be further explained that long tenure CEO tend to be reluctant to firm performance. According to Baron and Kenny (1986) the moderator should be significant with or without the moderation and from the findings it reveal a significant association on the dependent variable, this pave was for moderation. In Model 4 CEO gender is negatively and significantly associated with firm performance. Board member's independence is positive and significant to firm performance. CEO tenure is negative and significant to firm performance. While the interaction of CEO tenure on Board independence and firm performance is insignificant.

Table 6. Regression table.

Variables	Model 1	Model 2	Model 3	Model 4
Constant	4.976***(0.366)	4.787***(0.350)	4.771***(0.349)	4.820***(0.354)
CEO gender	-0.0223** (0.083)	-0.211*** (0.079)	-0.198** (0.079)	-0.196**(0.079)
Board size	-0.235(0.141)	-0.166(0.135)	-0.167(0.134)	-0.186(0.137)
Firm size	0.146 (107)	0.097(102)	0.098 (101)	0.096 (102)
Board independence		0.234***(0.038)	0.229***(0.038)	0.227***(0.038)
CEO tenure			-0.338*(0.032)	-0.310*(0.188)
Board independence* CEO tenure				0.151(0.188)
R^2	0.033	0.124	0.135	0.137
Adj R^2	0.025	0.115	0.123	0.123
F	4.132	12.975	11.424	9.618
Sig.	0.007	0.000	0.000	0.000

Note: *Significance at 10 %.
** Significant at 5 %.
*** Significant at 1 %.
Source: Research data 2022.

5. Discussion and Conclusion

Responding to the debate on firm performance, this study establish how CEO Tenure and board member's independence influence firm performance in private firms in Kenya. The intense competition in the Kenyan private sector has brought down some firms into their knees, for firms to survive in such volatile business environment, they should consider its performance. CEO and board members are at the fore front of ensuring that firm attains its optimal performance. The findings in Table 6 Model 4 further shows that independent board members are essential to increase firm performance this is consistent with the findings of other scholars (Foo & Zain, 2010; Liu et al., 2015). This findings are in support of resource dependency theory in that board members are full of unique resources that can facilitate firm performance.

CEO tenure in Model 4 reveals a negative significant relationship, this is in line with the findings of scholars who argue that long-tenured CEOs may have significant power over board member selection and cultivate personal relationships with board members (Walters et al., 2007). Eventually, such board members may learn to blindly trust their CEOs (Gentry et al., 2021; Guldiken et al., 2019). As a result of such a power shift, CEOs may pursue personal gains besides the interests of shareholders, including firm expansion in order to argue for higher financial rewards (Davis, Schoorman, & Donaldson, 2018), diversification of risks (Wang & Chen, 2020), and satiation of their own narcissism as such CEOs may not focus on firm performance thus reducing (Zhu & Chen, 2015). The interaction terms of CEO tenure on the relationship between board member's independence and firm performance in Model 4 indicate no association and thus insignificant.

5.1. Theoretical and Practical Implication

The study extends the argument on agency theory. The assumptions of agency theory are that CEOs have motives and that independent board members serve as an effective monitoring process to safeguard shareholders, constrain CEOs selfish motives actions, and mediate the principal-agent conflict (Shan, Liu, Chen, & Ma, 2023). This study extent the debate of having independent board members to safeguard shareholders interest and ensure continuous increase in firm performance. The practical implication is that firm to remain competitive and innovative firms should consider board member's independence. Therefore appointing board members who are independent guarantees firm performance.

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