THE RELATIONSHIP BETWEEN OWNERSHIP AND FINANCIAL PERFORMANCE OF COMPANIES QUOTED ON THE NAIROBI STOCK EXCHANGE (NSE)

BY

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D61/73485/2009

RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT FOR THE AWARD OF MASTER OF BUSINESS ADMINISTRATION (MBA) DEGREE OF THE UNIVERSITY OF NAIROBI

NOVEMBER 2011

DECLARATION

This research project is my own work and has not been submitted for award of any degree in any other university and where other people's research work has been used, they have been *duly acknowledged.*

Signed..... Date.....14/11/2011.....

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This research project has been submitted for examination with my approval as the university supervisor.

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LIST OF ABBREVIATIONS AND ACRONYMS

FDI - Foreign Direct Investments

FE – Foreign Equity

FO – Foreign Ownership

FOE – Foreign Owned Enterprises

IMF – International Monetary Fund

KenInvest – Kenya Investment Authority

MNC – Multinational Corporations

MNE – Multinational Enterprises

NSE – Nairobi Stock Exchange

R&D – Research and Development

ROA – Return on Assets

ROE – Return on Equity

TE – Total Equity

UK – United Kingdom

USA/US – United States of America

WTO – World Trade Organisation

ACKNOWLEDGEMENT

My sincere gratitude goes to the Almighty God for His protection and faithfulness during the entire course period.

I wish to highly express my gratitude to my Supervisor, Dr. Josiah Aduda whose invaluable guidance and insight made it possible for me to carry out the research study to its logical conclusion.

I also wish express my gratitude to the staff of the CMA and the NSE for allowing me to use their facilities for purposes of data collection. My family and friends deserve mention for their patience and encouragement during the entire course. For those not specifically mentioned, accept my sincere gratitude for your contribution and assistance in any way to make this project a success. May the Almighty God bless you.

ABSTRACT

The research study sought to establish the levels of ownership of companies on the NSE and how it affects performance of the companies. The study focused on how foreign or domestic ownership may have an influence on the performance of the companies. The ownership structure of companies is expected to influence performance of the companies and the drive by the Kenya government to encourage foreign ownership to spur economic growth and create jobs influenced the choice of the study area. The significant gains expected from foreign ownership of companies can only be exhibited by how well they are able to utilise resources for the common good.

Companies listed on the NSE have mixed ownership with some fully domestic owned while others have both foreign and local ownership. The level of ownership was measured on a scale of 1 with those with fifty–fifty ownership showing a ratio of 0.5 for local and 0.5 for foreign ownership. Empirical studies have shown mixed results with majority showing that foreign ownership has a positive influence on performance of firms and vice versa. Performance was measured by return on equity for all the firms over a five year span between 2005 and 2009.

The research established that foreign ownership has a positive influence on the performance of companies on the NSE. Domestic ownership was observed to have a negative influence on the performance of firms quoted on the NSE. Foreign companies have substantial investments in proprietary technology and knowledge, superior management skills and access to large amounts of capital. Domestic firms on the other hand are expected to have a home advantage brought about by social and cultural factors and political leverage.

The findings from the study may help improve policy development by the government as the results indicate that foreign ownership is able to create greater economic benefits for the shareholders. Probably, increased foreign ownership is what companies at the NSE should be seeking to enhance creation of shareholder value.

CHAPTER ONE
INTRODUCTION

1.1 Background to the Study

The focus of the Kenya government immediately after independence was the Africanisation of the economy to encourage the participation of Africans in economic activities. The foreigners controlled the economy in sectors as diverse as agriculture and services such as retailing, banking and insurance. The Kenya government became a major player in capital-intensive sectors such as transport, banking, telecommunication and tourism through nationalization of some of the businesses. Locals were encouraged to engage in production and commerce with the government providing government guaranteed loans to reduce the cost of loans for the locals. This program of transferring economic activities to the locals was the focus for the better part of the 60's and 70's in Kenya, (Njuguna et al., 2006).

The motives for nationalization were political, social as well as economic. It was a key policy of independent governments in Africa that the means of production, distribution and exchange, should be owned by the local people to allow for rational allocation of resources, planning and control of the economy, (Njuguna et al., 2006). Many governments believe that domestic ownership of productive resources or businesses enables people to exercise full democratic control over the means of generating income and provides an effective means of distributing income through the utilization of their skills to benefit themselves as opposed to situations where foreigners own businesses or resources, (Bellack, 2004).

1.1.1 Ownership

Domestic ownership is a situation where the citizens of that country control or own the economic resources in the country. Foreign ownership is the opposite of domestic ownership and refers to a situation where businesses or resources in a country are completely or majority owned by individuals that are not citizens of that country. It also refers to a situation where businesses whose headquarters are located in another country from where control is exercised own the resources in another country. Domestic

ownership therefore refers to a situation where the citizens own or control the resources of that country. The push for local ownership started falling with the fall of socialism in the late 1980's as the IMF advocated for more liberalized trade regimes in all countries through WTO, (United Nations Centre for Trade and Development, 2005).

The late 1980's were the years that the European and American governments waged a campaign for democracy in Africa and the former Soviet Union. With the collapse of socialism, the previous supporters of African governments in the form of grants and aid shifted their focus to the former socialist republics breaking away from the Soviet Union. This shift in focus led to less aid and forced the African governments to scale down their activities. During this period, the African governments could no longer sustain the high wage bills without western aid and massive lay-off of government workers resulted, (Central Bureau of Statistics, 2009).

Immediately thereafter, the call for governments to shift from commercial activities and leave business to private firms became the rallying call. The western donors and World Bank pressurised the state to stay out of areas in which the performance of state-owned firms was manifestly inadequate. The state should confine itself to those areas where access to large amounts of capital (which the state can provide or guarantee) was relatively important, where competition was less demanding, and where alternative governance arrangements may to some extent substitute for monitoring by owners. This shift by the government brought about the shift in policy and the focus now was on how to attract Foreign Direct Investments (FDI's), (Bellack, 2004).

The shift in policy from Africanisation to attracting foreigners to own productive assets in the country legitimized the proposition that foreign ownership may proffer greater benefits than local ownership. In the long-run, each firm that is capable of surviving competition will end up with an essentially close to optimal ownership structure and the impact of ownership on performance will remain largely unobservable in any society in which this process has been operating for some time, (Demsetz and Lehn, 1985). A firm's ownerships structure is itself subject to market pressures, so that the impact of

ownership on performance is more difficult to test in mature markets, (Demsetz and Lehn, 1985).

1.1.2 Nairobi Stock Exchange (NSE)

The Nairobi Stock Exchange started operations in 1954 as a voluntary association of stockbrokers registered under the Societies Act. Trading in shares at the NSE was largely a gentleman's agreement between trading parties and mainly involved professionals acting on behalf of their clients before the registration of the NSE in 1952. Immediately after independence, the NSE remained a depressed exchange in trading volumes as uncertainty regarding the policy of new independent African governments' scared investors. The first issue of shares through the NSE was in 1988 when the first privatization involving the sale of a 20% government stake in Kenya Commercial Bank happened. This privatization marked the start of robust growth for the NSE. Notably, in 1994 the NSE 20-Share Index recorded an all-record high of 5030 points on Feb. 18, 1994, ("History of the NSE," 2011).

Currently the NSE has 47 listed companies whose shares trade on the stock exchange. The exchange has also grown to incorporate trade in financial securities such as bonds issued by the government as well as the private sectors. The study was a survey of all the companies listed on the NSE. Public companies quoted on the NSE have substantial foreign ownership as evidenced by companies such as Safaricom, East African Breweries, Barclays (K) Ltd among others. These companies' are associated with superior performance evidenced by the increase in the price of their shares and high dividend payouts as compared to locally owned companies, ("Listed companies on the NSE," 2011).

Similarly, locally owned companies have been associated with the search for foreign owners or strategic investors to shore up their capital and improve performance. The search for foreign companies to invest in locally owned companies or strategic investors has permeated to companies owned by the government such as Kenya Railways, Panpaper Mills, Mumias Sugar among others. Most of these partnerships go through

bureaucratic government processes but eventually the government still ends up getting dubious foreign investors. The research study examined whether there is a positive relationship between ownership and firms financial performance.

1.1.3 Financial Performance

Performance refers to how well a company is using its resources to make profits or create shareholder value. Performance in general denotes the ability of a firm or business to achieve the stated objectives of the firm. There are common measures of performance divided into financial or non-financial measures. Financial measures of performance include operating income, earnings before interest and taxes, return on assets and net asset value, (Kihara, 2004).

Economists tend to think of profit as the measure of performance that best captures both the creativity (the revenue side) and the discipline (the cost side) required for survival in a market economy. In the long term, this is true, but in the short term, profits may be extremely volatile and subject to a number of accounting decisions, especially with respect to costs, that bear little relation to long-term performance. Aptly put, "costs are essentially static, since they encapsulate the past history of the company. Revenues are dynamic, reflecting the ebb and flow of economic activity, customer preference and pricing signals", (Frydman et al., 1997)

The study focused on whether the ownership of firms plays' any role in the development of a country and whether this can be an avenue for resource allocation in an economy. If foreign firms have superior performance than domestic owned firms, the government can use ownership of firms as an avenue for the transfer of not only superior skills and technology, but as an avenue to uplift the economic status of the citizens and the country as a whole. Through legislation, foreign owned firms can be restricted on the length of time they can operate in a country before going public to encourage domestic ownership of resources that guarantee the creation of wealth and benefit local citizens. There are numerous laws in Kenya that encourage local listing of companies to enjoy low tax rates, but these do not restrict full foreign ownership of businesses in the country.

1.2 Statement of the problem

Foreign companies and especially Multi-nationals report superior performance in countries where they operate as a result of having either superior technology, proprietary knowledge or getting the best human talent, (Berger et al., 2000). They are also able to exploit cost advantages by locating their operations in countries that have favourable investment climates for foreign companies such as lower taxes, unrestricted repatriation of profits and friendly investor services, (Davies and Lyons, 1991).

The focus by most developing countries of late has been how to attract as much Foreign Direct Investments as possible in order to create jobs and exploit available resources such as minerals and existing human capital. Developing countries are not able to realize fully the benefits of Foreign Direct Investments as the foreign owned companies are repatriating all their profits back home and a new headache for host governments such as transfer pricing to evade taxes through high expatriate pay, overpricing of inputs to their subsidiaries and highly priced obsolete technology. Studies done by researchers have shown that the superior performance of foreign owned firms is not guaranteed. Empirical evidence emerging on negative spillovers casts doubt on such issues, (Chung et al., 1996). This raises the question of whether, if the firms were domestic owned, would the negative spillovers be evident?

Kihara (2004), in her study of ownership structure and company performance concluded that there was no relationship between corporate performance and ownership structure. In the same study, she stated that where government ownership was concentrated, there was a negative impact on performance. The two observations seem to contradict each other and this study intends to resolve this contradiction by adopting a continuous variable measure of domestic and foreign ownership as opposed to the high and low measures of ownership in the study by Kihara. Odhiambo, (2006) found out that there is a positive relationship between foreign ownership and firm performance. The firms studied were those in the oil industry. Smaller performance gaps between firms of the same industry in a country exist as firm specific advantages are more similar, (Bellack et al., 2002). This hypothesis by Bellack may explain the reason for the results of the study by Odhiambo

(2006), which focused on firms in the oil industry in Kenya which are also majority owned by foreigners as opposed to domestic ownership. The sample by Odhiambo (2006), may therefore suffer the effects of same-industry firm specific advantages bias. This study will reduce this bias by studying all the firms listed on the NSE.

Olteti, (2001) found out that only foreign ownership affects performance of firms on the NSE. The study covered only those firms in the Main Investment Market Segment at the NSE with only two classifications of ownership as either high or low. Again, these results contradict those of Kihara in her study in 2004 where she found out ownership does not affect performance of firms. This study extends the above studies by modifying the measure of the ownership variable as a continuous variable stated as the ratio of foreign or domestic ownership to total equity. The study focused on all firms on the NSE to reduce the similarity effects of same industry firm specific advantages that reduce performance gaps in the study by Odhiambo, (2006). The study intended to resolve the contradictory results in the study done by Kihara, (2004) by reassessing the role of ownership on financial performance of firms on the NSE where a number of prominent IPOs have featured in recent years. The study adopts a partial correlation co-efficient model, (Greene, 1997), to measure the relationship among the variables as opposed to the summary statistics model used by all the other previous local studies. Government ownership in this study was categorized under domestic ownership for easier analysis of the results and not as a separate variable as done by Kihara, (2004).

1.3 Objectives of the Study

The main objective of the study was to identify the relationship between foreign ownership and firm's performance. The specific objectives of the study included;

i) Determine the relationship between ownership and company's financial performance for public companies on the NSE.

ii) Compare foreign owned and domestic owned firm's financial performance.

1.4 Significance of the Study

This study sought to determine the relationship between ownership and firm's financial performance. This study was significant to the following groups;

Investors

Investors can use the findings of the study to identify which firms to invest in at the NSE. If foreign owned firms post superior performance as compared to domestic owned firms, investors can discriminate against locally owned firms in their investments to get higher returns from their investments.

Investment Analysts

The study was also of importance to investment analysts and advisors who can use the results to identify firms to invest in on behalf of their clients. This will ensure that they are able to get better returns for their clients and therefore get more clients and build confidence among clients.

Government Policy Makers

The study can also inform government policy in the development of policies for attracting investments into the country. By highlighting the superior performance of foreign owned firms, the government can use this as a basis for justifying investments by foreign firms in the country and vice versa.

Local Researchers

The results can also benefit local researchers as it can form the basis or foundation for further research on the factors that make foreign companies perform better than domestic owned firms or vice versa.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter outlines the existing theories regarding the research proposal and support any new findings that the researcher may wish to add to existing knowledge. The first section reviews available literature on the topic as discussed by various authors as well as any theories available on the topic. The second part reviews any studies done by scholars on the topic, their findings and conclusions. It also attempts to identify the existing gaps between the previous studies and this study. The literature review forms a basis for the researcher to reduce the chances of just stating what already exists by aligning the study to solve an existing problem. The researcher expects to contribute some insight on how investors on the NSE can use the superior performance of foreign owned companies to increase their wealth.

2.2 Theoretical Literature Review

Recent statistics from the Kenya Investment Authority (KenInvest) indicate that the country attracted on average Ksh 150 billion in Foreign Direct Investments (FDIs) over the last two years. The Kenya government has been keen to attract foreign investments in the belief that they offer certain economic benefits by developing legislation targeting these investments and setting up of an authority (KenInvest), being key indicators of commitment, (CBS, 2009). Are these foreign investments the key to continued economic growth or is the Kenya government acting out of desperation to create jobs at all costs? While the role of FDI's is not the focus of this study, most foreign companies enter markets through government intervention as they seek the best investment destinations for their capital. It is worth noting that one cannot study foreign ownership of businesses in a country without incorporating FDI's or multinationals (MNC), (CBS, 2009).

Foreign investors play a major role in the emerging economies such as Kenya and have substantial holding in every major sector of the economy. Wherever these businesses are players, they have characteristically been outperforming all the local or domestic owned firms. In some sectors, these firms control virtually 95% of the assets in that sector and may be real monopolies, such as the cigarette and beer industries. In the financial sectors,

it is only recently that domestic owned firms have started to catch up with these MNC though the influence of foreign capital cannot be ruled out in the domestic owned firms such as Equity where the IFC holds some substantial stake. There are several theories advancing the view that foreign owned businesses post superior results as compared to domestic owned firms.

2.2.1 The General Global Advantage Hypothesis

The general global advantage hypothesis predicts foreign owned firms to be more profitable due to some comparative advantages that domestic owned firms lack, (Berger, Young and Genay, 2000). These advantages stem from advanced technologies, more efficient organizations due to stiff competition in the home market, a more active market for corporate control and better access to an educated labour force with the ability to adapt to new technologies. The home field advantage theory and the global advantage theory predict mutually exclusive results for the performance of foreign owned firms. A third theory overcomes this mutual exclusiveness of both theories, (Berger et al., 2000).

2.2.2 The Limited Form of the Global Advantage Hypothesis

This theory states that 'domestic banks are more efficient than foreign banks in most foreign countries, that domestic banks may be equally efficient as foreign banks from some countries, but that domestic banks may be less efficient than foreign banks from one (the United States) of the foreign countries' (Berger, Young, and Genay, 2000). The focus of this study is to determine the relationship between foreign ownership and firms' performance empirically. To test for the impact of foreign ownership on performance, the researcher used a continuous foreign ownership variable as opposed to the discrete variables used in most studies done locally. Foreign ownership relates to the level of control of the affairs of a business and the percentage of ownership is not itself a measure of control as some investors may appoint nominees to the board of directors who may not exercise full control. However, a foreign company for purposes of this study was that in which foreign citizens control more than 30% of the shareholding.

2.2.3 The Obsolescing Bargain theory

The theory proposes that the bargaining power of foreign companies is eroded over time and any superior performance noted could be attributed to entry behavior where the host country may go to great lengths to attract foreign companies as observed in FDI initiatives. The theory of obsolescing bargain predicts that the passage of time will result in erosion of the multinational's bargaining power, (Vernon, 1971). At the outset, multinationals enjoy a high degree of bargaining power since the host may want to attract it to the country on account of its capital, technology or marketing expertise. However, Vernon suggested that once the multinational has sunk its assets in a developing country, its vulnerability immediately increases. If the multinational's operations are highly profitable, the passage of time may reduce the government's appreciation of the up-front risks assumed by the company at entry. As a result, the perception is that multinational earn disproportionately high returns. Finally, political opponents persuade the government to reduce multinationals' power as a demonstration of its independence from foreign influence, (Jenkins, 1986).

The erosion of the multinational's bargaining power reflected in lower bargaining success, is a measure of how close the terms of the deal negotiated are to the multinational's objectives, as opposed to the host's objectives. Bargaining success is, in itself, difficult to measure, and multinationals' level of foreign ownership in local subsidiaries is a widely accepted proxy for level of bargaining success. Static bargaining success refers to the multinational's success in negotiations with the host government at a point in time, and is reflected in the level of foreign ownership at that time (i.e., a static phenomenon). Dynamic bargaining success refers to its success in preventing erosion of the terms of its deal with the host over time, and is manifest in the proportion of foreign ownership retained by the multinational over a period of time (i.e., a dynamic phenomenon), (Davies et al., 1991).

Davies and Lyons (1991) suggest that three moderating forces affect bargaining success. These forces include the political climate in the host country, host's perception of value associated with the multinational's operations and multinational's ownership preferences. Literature on the obsolescing bargain suggests that a number of company-level primary

variables that simultaneously affect more than one force drive these forces. There can be great differences in host governments' attitudes towards multinationals, both across countries and within a country at different periods. An example is the Taiwanese and Korean governments' attitudes towards multinationals that has changed drastically over the years, (Wade, 1990). These changes driven by ideological transformations, i.e., a shift from an inward-looking socialist posture in which the government resents foreign control of domestic assets, to one leaning towards the free market system and welcomes the contribution of foreign capital. With time, the host's view of multinationals' contributions can change depending on the extent to which the multinational's contributions are rooted in image, rather than value. Emergence of local competitors whose activities substitute for the value contributed by the multinational, Vachani (1990), the "sunk" nature of the multinational's investment and host's political climate and the multinational's ownership preferences (e.g., a multinational seeking high ownership levels may be viewed with suspicion, and that may reduce the value perceived to be attached to its activities), (Vernon, 1971).

Gomes (1990) has noted that the evolution of the bargain between the multinational and the host government affects the multinational's ownership preferences. These ownership preferences are determined by numerous factors such as trade-offs between equity and non-equity benefits, size of the firm, nature of intangible assets, cultural and other historical ties between the host and home countries, export performance and control preferences typical of managers in home country companies. The political climate the company finds itself in affects a Companies' ownership preferences, (Gomes, 1990).

2.2.4 The Specific-Advantage Hypothesis

The specific-advantage hypothesis is at the centre of the economic theory of the MNE and argues that the existence of MNEs hinges on the nature of the specific advantage of the firm, (Dunning et al., 1973). The MNE transfers firm-specific advantages denied competitors internally across borders becoming their competitive edge. MNEs will therefore be concentrated in knowledge-intensive sectors, which are generally characterised as growth- and high-productivity industries. Markusen (1995), states that multinationals tend to be important in industries and firms with four characteristics.

These characteristics include high levels of R&D relative to sales, a large share of professional and technical workers in their workforces, products that are new and/or technically complex and high levels of product differentiation and advertising'.

The incentive to internalise the advantage for MNEs stems from the possibility of market failures when contractual market transactions are used. The mobility stems from the intangible nature and leads to low marginal cost when the advantage is used in an additional affiliate abroad. The specific advantage hypothesis states that the firm-specific advantage compensates for disadvantages that a foreign entrant into a market has some disadvantage vis-a`-vis established firms, (Koutsoyiannis, 1982). In essence, the specific advantage can therefore explain the performance gaps that make foreign firms better performers as compared to domestic firms. This argument is consistent with the notion that MNEs possess assets, where imitation by competitors is very difficult and diffusion therefore slow. The Industrial Organisation (IO) view of the MNE focuses on the fact that MNEs enter a market abroad to exploit optimally their firm-specific advantage. Contrary to the specific-advantage hypothesis, here firm-specific advantages are not given. The IO-approach argues that the firm-specific advantages referred to above, arise as a product of oligopolistic rivalry, (Acocella, 1992).

2.2.5 World Best Practice View Model

An alternative model is the world best practice view in which FOE's are representative of the best practice technology that is available in their country of origin (German machine tool producers, Japanese electronics firms etc.) as proposed by Davies and Lyons (1991). They noted that it is not necessary for foreign owned firms to be significantly more efficient than their domestic counterparts who do not produce overseas as entry barriers limit penetration in the host economy and the size of the market combined with economies of scale. They postulated that aggregate UK manufacturing productivity would be raised by as much as a quarter by moving to world best practice. The best practice hypothesis suggests that the foreign firm's advantage when producing in a host country positively correlates with the international productivity differential between its parent country and the host country. The authors concluded that with appropriate management, foreign owned firm's productivity levels are potentially attainable by

domestic firms as a possibility taken seriously. MNEs are not simply a firm specific idiosyncrasy, but display features which are dependent on industry and nationality, (Davies and Lyons, 1991).

2.2.6 The Home Field Advantage Hypothesis

This hypothesis proposed as an alternative to the global advantage hypothesis proposes that domestic owned firms possess some home field advantage. Berger, Young and Genay in 2000 formulated the home field advantage hypothesis in their study of the different impacts foreign and domestic ownership have on bank performance. The hypothesis predicts that domestic owned firms are more profitable due to the absence of the structural agency costs that foreign owned banks confront. Distance between the principal, the parent firm in the home country, and the agent, the subsidiary or branch in the host country, creates a cost for the foreign firm that relates to operating or monitoring the subsidiary or branch from a distance. Other factors leading to a comparative advantage for domestic firms were differences in language, culture, regulatory and supervisory structures between the home and the host country of the foreign firm, (Berger et al., 2000).

2.3 Corporate financial performance

The narrowest concept of business performance centers on the use of simple outcome based financial indicators that assumed to reflect the fulfillment of the economic goals of the firm. This concept referred to as financial performance has been the dominant model in empirical studies on business performance. Typical of this approach involves examining such indicators as sales growth, profitability reflected by ratios such as return on investment, return on sale, and return on equity and earnings per share among others, Hofer, (1983).

Hax et al. (1984), reflecting on the popular and current view that "market" or "value-based" measurements are more appropriate than accounting- based measures employed such measures like market-to-book value or stock-market returns and its variants. The primary distinction made among the many alternative measures is between measurements of accounting and economic profits, (Hirsch, 1991). Economic profits represent the net

cash flows that accrue to shareholders that represent capital (stock) market returns. Accounting profits can differ from economic profits due to timing issues, adjustments for depreciation, choice of accounting method, and measurement error. Additionally, economic profits are forward-looking and reflect the market's perception of both potential and current profitability, but accounting data reflects a historical perspective. Although there is widespread agreement in the literature that capital market measures are superior to accounting data, accounting data provides additional relevant information, (Hirschey et al., 1984).

Other measures of financial performance include the Tobin's Q, the ratio of the market value of a firm to the replacement cost of its assets (Lindberg et al., 1981). This approach remains financial in its orientation and assumes the dominance and legitimacy of financial goals of a firm by using the current market value of a firm as a ratio of its market value of its assets. This departure from the traditional accounting and financial indicators that may use historical data skews the results of any analysis of financial performance, (Lindberg et al., 1981).

A broader conceptualization of business performance would include emphasis on indicators of operational performance (non-financial) in addition to indicators of financial performance. Under this framework, it would be logical to treat such measures as market-share, new product introduction, product quality and marketing effectiveness, manufacturing value-added and other measures of technological efficiency within the domain of business performance. Similarly, market-share position, widely believed to be a determinant of profitability would be a meaningful indicator of performance within this perspective. The inclusion of operational performance indicators takes us beyond the "black box" approach that seems to characterize the exclusive use of financial indicators and focuses on those key operational success factors that might lead to financial performance, (Buzzell et al., 1975).

2.4 Ownership

Different ownership types differ due to the interests and constraints of owners and managers, the abilities of these parties to obtain resources from product markets and

factor markets, such as capital, management and technical talent. Ownership may be individual, institutional or government-owned. Individual ownership refers to a situation where all or some of the shareholding is owned by individual shareholders. Domestic private ownership refers to ownership that is domestic by private individuals or private companies. Governments also own shares in companies that exhibit high technological, capital and skilled labour outlays, (Griffith and Simpson, 2000).

Foreign ownership is different as it is mainly private and not state-owned. Private foreign firms are most apparent in industries that are competitive in most of the world and are usually associated with higher productivity, (McGuckin et al., 1995). A great deal of research has found that private firms are more efficient than state-owned firms are, and that firm performance improves after privatisation. Foreign firms often have access to superior technology, greater access to export markets, and new management techniques. Moreover, foreign owners tend to be large shareholders, who can internalize the costs of monitoring and tend to devote greater efforts to monitoring. As a result, the CEO works harder, and firm performance improves, (Davies and Lyons, 1991).

A combination of three sets of factors drive ownership preferences of MNE's. First is the relative capabilities of the MNE's and host country's firms which affect potential benefits of cooperation between firms. The second factor is the transaction cost of transferring each partner's capability to a cooperative venture. When the costs of using contractual channels are high for both partners contributions, ownership channels preferred are joint venture between domestic and foreign firms. The third set is the special costs of joint venture resulting from shirking by partners and increased management costs due to conflict of interest, (Gomes, 1990).

Government-owned firms have generated much controversy about "unfair-competition" in such diverse industries as airlines, telecommunications, mining, aircraft manufacturing and steel. State-owned firms in developing countries shielded from competition are inefficient, and often end up receiving a constant flow of subsidies to stay afloat. Foreign parents of different ownership types may possess different ownership advantages. If ownership advantages such as management and marketing skills, technology, and capital

play crucial roles in the success of foreign-controlled firms, we would expect a lower failure rate from foreign controlled firms than those controlled by domestic firms, (Gomes, 1990).

The ownership effect might be due to 'pure' efficiency and technology differentials, but it might equally be due to differentials in labour skills, capital input, vertical integration or monopoly power in the product market. Another possibility is that measured productivity differences are the result of transfer pricing which artificially inflates measured FOE productivity. Similarly, the structural effect might be a matter of history or essential industrial structure, which current managerial policy cannot alter, but the choice of industry, might equally be a key function for strategic management and the quality of such choices relate to nationality of ownership, (Harris, 2002).

2.5 Empirical literature review

The empirical review is concerned with studies done by other scholars in comparing the performance of foreign companies and domestic owned firms. It is important to note that most of these studies conducted were either in developed countries or in the emerging economies of Asia and Latin America. The differences between developed and developing countries that are likely to affect the performance of foreign companies are expected to be in favour of foreign companies operating in developing companies as domestic companies are likely to be less competitive. The history of domestic companies in developing countries is less and they are likely to be technologically weak, small, have high operating costs as well as low economies of scale. This will affect their performance though this is not supposed to be an excuse for the continued protection by governments. The recent push by governments to attract FDIs to attain economic growth is a cause of concern for domestic firms to improve their production capabilities as the world economy becomes global. This paper cites the studies done locally and other countries though studies in developed countries dominate published studies.

Kihara (2004), in her studies of ownership structures and firm performance of firms listed on the NSE found out that there was no relationship between firm performance and ownership structure. The focus of her study was on the extent of concentration of

ownership and firm performance where she found no relationship. These findings seem to contradict the findings of Olteita (2001), in a study of 15 firms listed on the Main Investment Segment of the NSE. Olteita found that there was a relationship between ownership structure and firm performance. Indeed, Olteita used discreet variables for ownership and was able to establish a relationship between firm performance and ownership structure. The sample for Olteita was quite small and may not have been representative enough as firms in the study segment are capital and technology intensive. This segment is a major attraction for governments, institutional and foreign investors and may be the reason for positive relationships.

Majnoni, Shankar, and Várhegyi (2003), in their study of banking industry in Hungary concluded that during the period 1994 to 2000, foreign banks in Hungary were able to achieve a consistently higher profitability than domestic banks. The authors argue that this higher profitability relates to the length of time the foreign bank is present in the host country and to the nature of the establishment. In addition, the authors find greenfield investments outperforming other forms of entry of foreign banks. Sabi (1996), also concludes that foreign banks in Hungary are more profitable than domestic banks.

A descriptive study by Naaborg et al. (2004) shows that during the period 1995 to 2000, the Return on Assets (ROA) of foreign banks in eight transition economies was lower than that of domestic banks. The authors found out that the ratio of overhead costs to total assets hardly differs between domestic and foreign banks. A descriptive study by Crystal, Dages, and Goldberg (2002), shows lower ROA for foreign banks in Argentina, Chile and Colombia. The authors point at higher provisioning of foreign banks as an explanation. Based on a very preliminary cross-country study, Lang and So (2002), find that ownership structure has no impact on economic performance of banks. They concluded that the general belief that foreign ownership can help to improve performance of banks in emerging markets is not supported by empirical evidence.

Rajah and Ashish (2008), in their study of foreign ownership, technological intensities and economic performance of automotive parts firms in India observed that there is a strong positive correlation between technological intensities and labour productivity of

firms in the study. This link obviously supports the evolutionary argument that embodied technology as important in competitiveness as firms with higher technological intensities show higher labour productivity. There was a high coefficient of technological intensities among local firms which indicated that local firms produce more technological effort at host sites than foreign firms, which is consistent with Dunning's (1974), arguments on asset specific advantages as the latter enjoys access to superior product technology from parent plants.

Davies and Lyons (1991), in their study of the productivity advantage of foreign owned firms in the UK found out that foreign owned firms' superior productivity might be due to differentials in labour skills, capital input, vertical integration or monopoly power in the product market. Another possibility could have been that measured productivity differences were the result of transfer pricing which artificially inflated measured foreign owned firms productivity. They also noted that the structural effect might be a matter of history or essential industrial structure that current managerial policy cannot alter, but the choice of industry might equally be a key function for strategic management and the quality of such choices relates to nationality.

The main explanation of productivity gaps is no different from explanations relating to the existence of multinational firms, (Bellack, 2004). The author concluded that the productivity gap therefore is more a firm or plant-specific phenomenon, rather than industry related. There is a size effect reported in many studies, larger firms either domestic or foreign owned acquire low productivity firms, (Feliciano and Lipsey, 1999). Besides ownership factors, a first additional source of productivity gaps are differentials in the mix of activities undertaken by foreign owned firms and domestic firms, (Globerman et al., 1994). Foreign owned firms undertake a set of activities different from those pursued by domestic owned plants. This makes them perform better such as in the case of a higher degree of specialization, research and development units which employ highly trained staff or highly-automated production facilities, which require highly qualified blue-collar workers and have above average skill levels, (Globerman et al., 1994).

Maliranta, (1997) and Oulton, (1998) have noted that the failure of domestic producers to adopt 'best practice technology' or 'frontier technology' has been a source of the rise in productivity gaps. Inferior access to technology by domestic owned firms may have several explanations such as their smaller geographical range of operation or their absence from certain markets, lacking the possibility to tap into the local knowledge-base abroad or not profiting from regional agglomerations. They might not have the necessary information or they may lack the capability to make efficient use of acquired technology, related to organisational learning processes and path dependence, (Davies and Lyons, 1991).

Another source of productivity gaps is simply a higher input intensity per worker, which relates to capital or technology-intensity. Girma et al. (2001), concludes that the substantial productivity gaps ascribed to foreign ownership declines to 5% after controlling for labour productivity. Globerman et al. (1994), shows that the gap vanishes once they control for size or capital intensity. Oulton (1998), studied productivity gaps in the UK and found out that in the manufacturing sector, labour productivity is 38% higher in foreign firms due to their higher capital intensity (physical and human). In service industries where Oulton examined over 49,000 companies, a productivity gap of one third over domestic firms' productivity remained after controlling for various structural differences such as size, age and parent country. Again, a more skilled labour force and a higher capital-intensity in foreign firms explain most of the variation. Using a different methodological approach Griffith et al. (2001), point out that the same factors matter, namely skill intensity, size and capital intensity, yet they explain very different proportions of the variation in the three industries examined.

While some controversies have existed in the area of comparing the performance of foreign owned companies and domestic companies, there is conclusive evidence that foreign owned firms tend to perform better than their domestic siblings are. Using a sample of UK car firms and distinguishing between acquisition and greenfield entry, Griffith (1999), finds relatively small differences in total factor productivity and foreign firms are not more productive than UK domestic firms in various subsectors are. Harris (2002), repeats the estimation of Griffith (1999), and using the same methodology, finds

the opposite results on the plant level, namely that productivity gaps do exist. Girma et al. (2001), focusing on the UK manufacturing sector included total factor productivity and found a growth differential between domestic and foreign firms. Griffith and Simpson (2000), building on Griffith (1999), extended the analysis to the total manufacturing sector, dividing foreign firms into 'always foreign owned' and into 'foreign owned taken over' (changing ownership). The authors report gaps of total factor productivity between these two groups, depending on whether one looks at levels or growth rates. They also find a skills gap in line with the productivity gap.

De Backer (2002), in a study of MNEs in Belgium, after controlling for a number of standard variables, explains the large productivity gaps by scale and technical efficiency. Being able to single out the Belgian MNEs and foreign owned MNEs, his findings show a greater similarity between these two groups than to uni-national Belgium firms. In addition, foreign owned firms and domestic owned firms may make different use of public infrastructure (including the institutional environment, national systems of innovation etc.). The particular configuration of firm-specific advantages and location advantages may be superior for foreign owned firms, since they invest and divest plants continuously in different environments abroad. Thus, their distribution of plants across locations could reflect a better match than that of uni-national firms, (De Backer, 2002).

An additional source of productivity gaps identified by the literature concerning acquisitions, namely, that foreign firms may be particularly good at 'picking the winner', frequently also termed as 'cherry pickers' (Oulton, 1998). The 'restricted matching hypothesis' by McGuckin and Nguyen (1995), states that firms with above average productivity are taken over, finds support in many studies. Yet, it is difficult to establish cause and effect and in most cases, it is not clear, whether domestic owned firms or foreign owned firms or both are involved. An exception is evidence provided by Moden (1998), who reports that it is primarily high productivity firms acquired by foreign firms in Sweden. Moden (1998), studied post-acquisition productivity focusing on foreign acquisitions in Sweden. He found that while foreign acquisitions have increased labour productivity, the development of total factor productivity is more uncertain which he attributed to time effects. Such results interpreted in the light of the 'restricted matching

hypotheses, yet seem largely to depend on firm size and on the initial productivity level, (Moden, 1998).

2.6 Summary of Literature Review

It is evident from the existing theories and hypothesis regarding foreign ownership and performance that in most cases, foreign firms show better performance than local firms do. The superior performance, though caused by the interaction of different factors is an undeniable fact. The foreign firms (MNEs), usually have a lot of advantages over the domestic firms such as their superior technology, their size and market share, proprietary knowledge and highly skilled and knowledgeable workers among others. They could also be posting superior results due to the capital intensity of the industries in which they invest in and entry advantages accorded foreign companies by the host governments. These factors coupled with globalization and the WTO rules on world trade have led to the dominance of markets by MNEs and foreign firms.

Kenya being a developing country is in an extremely vulnerable position as domestic companies have little in terms of technical expertise or proprietary knowledge. The domestic firms cannot therefore be better performers due to their size and history especially at the national level. While the government may do all in its power to protect the local industries, there is no evidence that this has succeeded. In retrospect, foreign companies have been able to acquire many concessions in operating in developing countries through preferential treatment in FDI initiatives. Local studies done by a number of researchers seem to contradict this widely held view as evidenced by Kihara (2004) and Oltieta (2001) and this study will seek to put to rest this contradictions.

As stated earlier, different scholars and authors have reported conflicting results relating to ownership and firm performance. This study aimed to contribute to the debate by carrying out an empirical test on firms quoted on the stock exchange to establish whether indeed, foreign owned firms report better performance than domestic owned firms do. Return on equity (ROE) based on profit before taxes was used to measure financial performance, and related to domestic and foreign ownership levels. The focus of the study was companies listed on the NSE.

CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction

This chapter outlines the research methodology, selection of the study population, selection of the sample, data collection instruments and data collection procedures and data analysis. It outlines how the researcher carried out the study to achieve the study objectives.

3.2 Research Design

The research study adopted a causal research design that focused on the effect of ownership on financial performance. Empirical studies have shown that those firms that have substantial foreign ownership are likely to report better performance. However, other studies have reported the opposite result stating that there was no significant relationship. The study intended to determine how a firm's financial performance relates to the extent of foreign or domestic ownership of firms quoted on the NSE and. The adoption of the design ensured proper representation of all the sectors as most of the studies done previously were sector specific or panel based. Firms quoted on the stock exchange represent a mixture of both foreign as well as domestic owned firms and are therefore likely to be a representative of firms across the Kenyan economic landscape.

3.3 Population and Study Sample

The research population represents the elements studied in the research. They consisted of all the 46 firms quoted on the Nairobi stock exchange, as information for these firms was easily available. The country has substantial numbers of firms that are foreign owned in all sectors of the economy. However, as most of these firms are private, the determination of their true ownership may be a problem and this informed the study to focus on public firms whose ownership was easy to establish. The researcher carried out a survey of all the firms quoted on the NSE and therefore no need for sampling the firms.

3.4 Data Collection Methods

The data collected in this study to determine financial performance was obtained from accounting data contained in company annual reports 2005-2009. The data relating to ownership was also obtained from the annual reports of the listed companies. Listed companies are required by disclosure requirements specified under the CMA act and those prescribed by the Financial Reporting Standards to disclose their shareholding structure. This information is also disclosed by companies in their annual reports under the corporate social responsibility policy. The reports were available from the NSE handbook and the CMA library.

3.5 Data Analysis

The ownership levels were determined by stating foreign ownership and domestic ownership capital as a ratio of total capital of the firm, (Gomes, 1999) . The financial performance of the firm was determined as the return on equity, (Hofer, 1983). To determine the relationships between the variables, linear regression model using the ordinary least squares method was used. The linear regression model is suggested by Greene, (1997) and is based on the Tobit model stated as follows;

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \ldots\ldots + \beta_n X_n + \varepsilon$$

Where Y represents firm's financial performance measured as the return on equity, β_0 represents the intercept or constant, $\beta_{1\ldots\ldots}\beta_n$ represents the different co-efficients for the independent variables, $X_{1\ldots\ldots}$ X_n represents the independent variables. The regression model has two indendent variables, X_1 represents Foreign Ownership measured as a ratio of foreign equity divided by total equity of a firm , X_2 represents domestic ownership measured as the ratio of domestic owned equity divided by total equity and ε represents the error term or performance that ownership could not explain.

Financial performance of the firm was determined using return on equity for the firms in this study. This information obtained from the financial statements of the companies and based on the profits before tax in order to exclude the tax differentials that originated from different tax incentives given to listed companies on the basis of listed shareholding.

To generate the regression equation, the researcher used the Statistical Package for Social Sciences (SPSS) version 16. To determine whether the results are significant especially for achieving objective 2, tests of significance were computed. The researcher did not collect any invalid or unreliable data as the data was mainly secondary and tests of validity or reliability were unnecessary.

CHAPTER 4

DATA ANALYSIS AND PRSENTATION OF FINDINGS

4.1 Introduction

This chapter presents data collected during the study and analysis of the same. A total of forty six (46) companies were considered in the study and the data on their ownership and performance was collected. Ownership was a ratio of domestic or foreign capital to the total capital of a company with a total result of one for overall ownership. The performance of the companies was measured in terms of return on equity determined by taking the average of five years performance between 2005 and 2009.

4.2 Summary Statistics

The summary statistics for the study were computed and table 1 is a representation of the summary statistics output.

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation	Variance	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
Foreign ownership ratio	46	.01	.82	.3415	.26829	.072	.065	.350	-1.410	
Domestic ownership ratio	46	.18	.99	.6585	.26829	.072	-.065	.350	-1.410	
Return on equity	46	-.06	.70	.2392	.15370	.024	.879	.350	1.001	
Valid N (listwise)	46									

Table 1

Source: Research data analysis

From the output, the number of companies in the study was forty- six (46) as earlier indicated. The results show that the maximum foreign ownership was 82% while the minimum was 1%. The maximum and minimum levels for domestic ownership were

99% and 18% respectively. The average level of foreign ownership was 34.15% while the average domestic ownership level was a respectable 65.85%.

On performance, the average level of performance for all the companies was 23.92%. The standard deviation for performance was 15.37% implying that the difference between poor performers and good performers was not very wide. This may be an indicator that the companies are facing the same macro-economic environment and therefore report the same level of performance for all sectors of the company.

4.3 Foreign Ownership and Financial Performance

To test the relationship between the independent and dependent variable, a scatter plot for each of the independent variables against the dependent variable was drawn. The scatter plot is the first step in determining the nature of the relationship between the study variables. Foreign ownership and financial performance may have a positive relationship as indicated by the slope of the curve in chart 1.

Model Summary

R	R Square	Adjusted R Square	Std. Error of the Estimate
.325	.106	.085	.147

The independent variable is foreign ownership ratio.

Table 2

Source: Research data analysis

From the model summary, it is clear that foreign ownership can explain 32.5% of the variation of the dependent variable while the other variation depends on factors other than foreign ownership. However, the correlation coefficient that measures the strength of the relationship between the two variables shows a weak but positive relationship at 0.1.

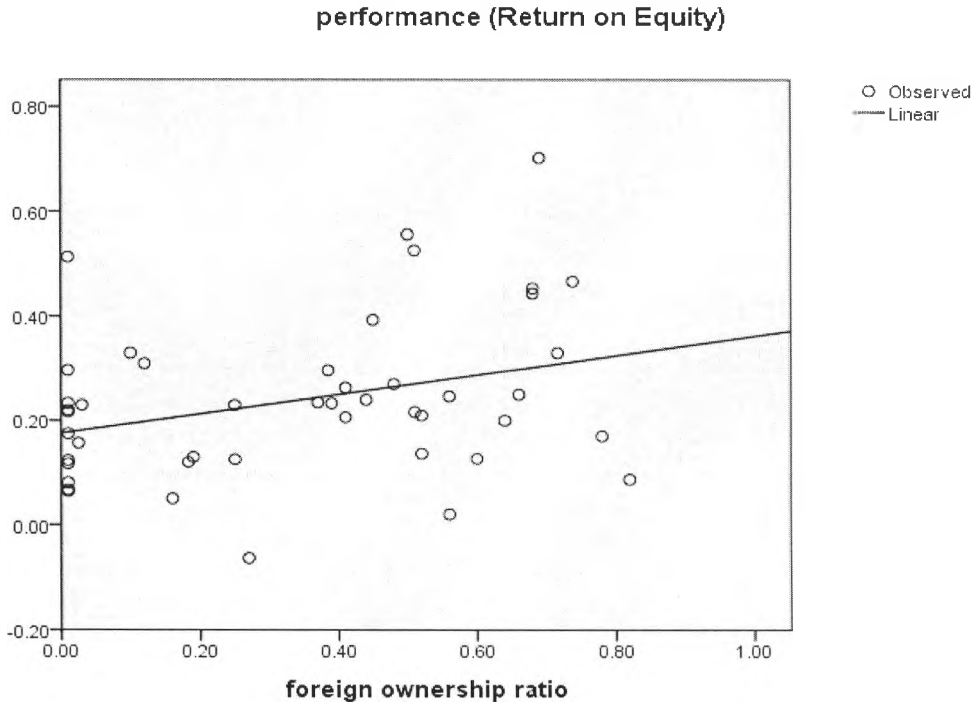

Chart 1
Source: Data analysis

Chart 1 shows that there is a relationship between foreign ownership and financial performance. As the level of foreign ownership increases, the level of financial performance also increases.

ANOVA

	Sum of Squares	df	Mean Square	F	Sig.
Regression	.112	1	.112	5.197	.028
Residual	.951	44	.022		
Total	1.063	45			

Table 3
Source: Data analysis

From the results measuring the significance of the variable, the results indicate that foreign ownership is a significant variable. The p value or significance at .028 indicated that foreign ownership is significant at 95% confidence level. This value is less than .05

indicating that for individual significance, the foreign ownership variable is significant. The coefficients for the partial regression equation on foreign ownership are 0.176 for the constant and 0.186 for the co-efficient of Foreign ownership as indicated by table 4.

Coefficients

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
foreign ownership ratio	.186	.082	.325	2.280	.028
(Constant)	.176	.035		4.974	.000

Table 4
Source: Data analysis

4.4 Domestic Ownership and Financial Performance

From the model summary, table 5, it is clear that domestic ownership on its own explains 32.5% of the variation of the dependent variable while the other variation depends on factors other than domestic ownership. However, the correlation coefficient that measures the strength of the relationship between the two variables shows a weak but positive relationship at 0.1.

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.325[a]	.106	.085	.14700

a. Predictors: (Constant), domestic ownership ratio

b. Dependent Variable: performance (Return on Equity)

Table 5
Source: Data analysis

The results measuring the significance of the variable in table 6 indicate that domestic ownership is a significant variable. The p value or significance at .028 indicated that

domestic ownership is significant at 95% confidence level. This value is less than .05 indicating that for individual significance, domestic ownership variable is significant

ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.112	1	.112	5.197	.028[a]
	Residual	.951	44	.022		
	Total	1.063	45			

a. Predictors: (Constant), domestic ownership ratio

b. Dependent Variable: performance (Return on Equity)

Table 6

Source: Data analysis

Domestic ownership and financial performance relationship coefficients are indicated in the co-efficients' table 7. The partial regression equation has the coefficients 0.362 for the constant and -0.186 for the domestic ownership variable. The negative coefficient for the domestic ownership variable is an indication of negative correlation with financial performance. The coefficients output indicated that both the domestic variable and the constant are significant in the equation as the p value is small at below .05. The variables of domestic ownership and financial performance can be included in the equation showing the relationship between the two.

Coefficients

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
domestic ownership ratio	-.186	.082	-.325	-2.280	.028
(Constant)	.362	.058		6.240	.000

Table 7

Source: Data Analysis

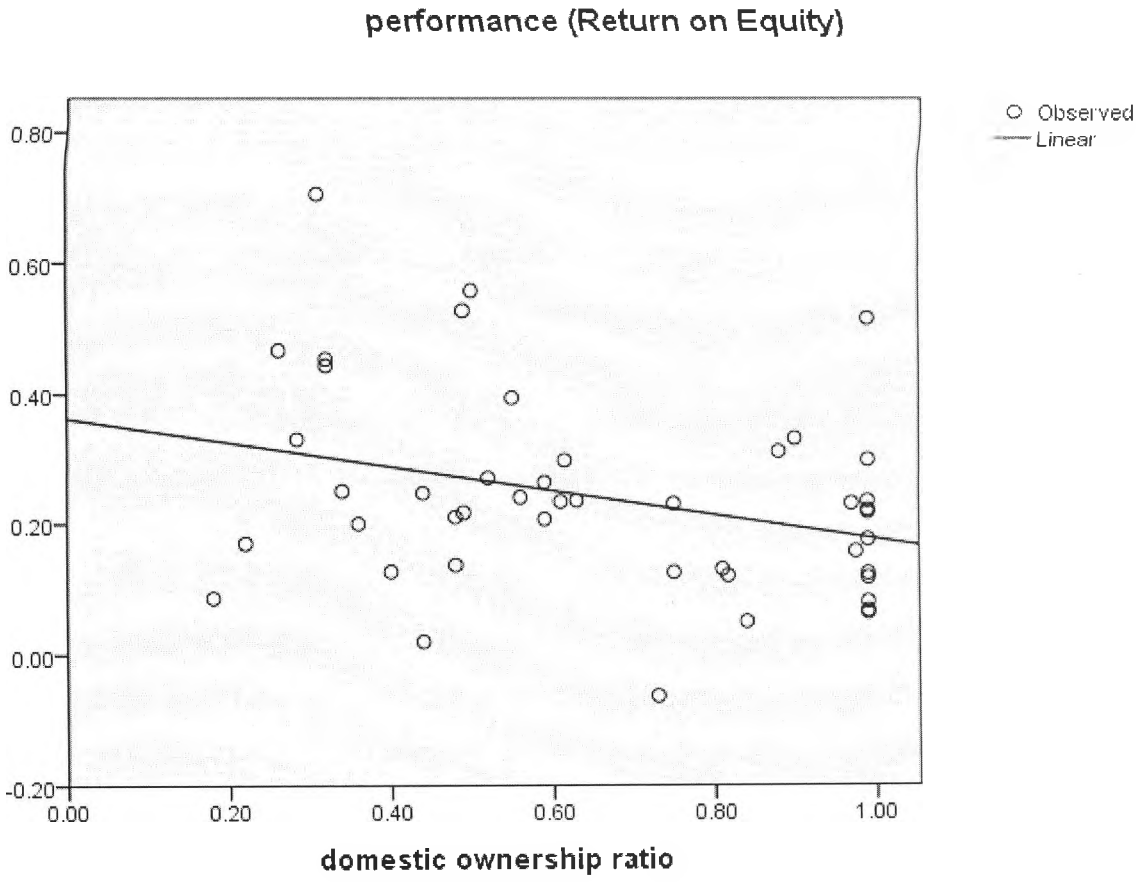

Chart 2
Source: Data analysis

Chart 2 shows that there is a relationship between domestic ownership and financial performance. As the level of domestic ownership increases, the level of financial performance decreases. The data does not assume the bell shape that indicates a decreasing or increasing variation making it a more stable predictor of financial performance as compared to foreign ownership.

4.5 Summary and Interpretation of Findings

The research indicated that the ownership of companies at the NSE is in favour of domestic ownership. This may be an indication of the high levels of risk associated with emerging markets and the reluctance of foreign investors to invest in emerging markets. Developing countries are associated with high political and economic risks and investors

expect a higher rate of return for their investment. This rate of return may not be evident especially in companies that have substantial local ownership therefore discouraging foreign ownership.

The study established that there might be a relationship between ownership and financial performance of a firm. An interesting fact that emerged was the negative relationship between domestic ownership and financial performance of firms. As the level of domestic ownership of firms increased, the financial performance of firms went down. Domestically owned firms are expected to exploit their knowledge of the domestic market and post superior results but this is not empirically evident for companies quoted on the NSE. Indeed, firms with substantial local ownership are observed to post poorer results than their foreign owned counterparts.

From the data analysed, it is clear that that companies listed on the NSE are majority owned by the locals and not foreigners. Foreign ownership is positively skewed which implies that the scatter graph for this variable and performance is positively inclined as opposed to the skewness of domestic ownership which is negative. Domestic ownership seems to have a negative impact on financial performance while foreign ownership has a positive influence on financial performance.

The summary model regression equation for predicting the financial performance of a firm excludes the foreign ownership variable to reduce data redundancy. One key observation is that the data assumes a bell shape as the level of foreign ownership increases, indicating that the variance of the residuals increases. This is a case of existence of heteroscedasticity or multicollinearity and further analysis is necessary to determine the nature of the relationship. This may be because a measure of the foreign ownership variable has an effect on the domestic ownership as both variables add up to 1.

The variation relating to the regression or variation explained by ownership is 11.2%. The rest of the variation of 88.8% therefore relates to other factors other than the predictor variables. The role of the predictor variables is therefore weak though there is

an indicator of some influence on financial performance of firms. The equation therefore adopts the partial equation for domestic ownership, as it is more dominant of the two variables. The statement of the regression equation is stated as follows;

The regression equation summarises the findings for the whole study showing that company's performance will be influenced by ownership and other factors upto 63.8%. The constant or the equation is .362 or 36.2%. It indicates that firm's financial performance attainable without including other variables is about 36%. The rest 63.8% will be influenced by the ownership factor in conjunction with other factors that were not the subject of the study.

The main observation that emerges from the study is that the two variables are individually significant. Each variable has an effect on the financial performance of the firms. While domestic ownership has a negative effect on financial performance, foreign ownership has a positive influence on financial performance. This indicates that increase foreign ownership will encourage creation of shareholder value and the converse is true for domestic ownership.

CHAPTER FIVE
SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary of the Study

The research study sought to establish levels of ownership of companies on the NSE and its effects on companies' financial performance. The recent push by the government of Kenya to offer incentives to foreign investors in order to attract Foreign Direct Investments was a key incentive for the study. Most developing countries are seeking foreign investments as a key economic driver. The foreign companies provide benefits to the local economy that domestic companies cannot provide.

The study focused on how foreign or domestic ownership may have an influence on the financial performance of the companies. The ownership structure of companies influences financial performance of the companies and the researcher sought to determine whether there is a relationship between ownership and financial performance. The significant gains expected from foreign ownership of companies exhibited by how well they utilise resources for the common good. Since resources are scarce, a country should ensure that the process of allocation favours the most efficient users and if these are foreign owned, they should get the resources.

Companies listed on the NSE have mixed ownership with some fully domestic owned while others have both foreign and local ownership. The level of ownership was measured on a scale of 1 with those with fifty–fifty ownership showing a ratio of 0.5 for local and 0.5 for foreign ownership. Empirical studies have shown mixed results with majority showing that foreign ownership has a positive influence on performance of firms and vice versa. Measurements of financial performance by return on equity over a five-year span between 2005 and 2009 and the average determined.

The research established that foreign ownership has a positive influence on the performance of companies on the NSE. The study observed domestic ownership has a negative influence on the performance of firms quoted on the NSE. Foreign companies

have substantial investments in proprietary technology and knowledge, superior management skills and access to large amounts of capital. Domestic firms on the other hand have a home advantage brought about by social and cultural factors and political advantage.

The findings from the study may help improve policy development by the government as the results indicate that foreign ownership is able to create greater economic benefits for the shareholders. Probably, increased foreign ownership is what companies at the NSE should be seeking to enhance creation of shareholder value.

This is in contrast to the relationship observed for foreign ownership. The observation made was that as foreign ownership levels increased, the financial performance of the firms also increased. This is in line with the various theories of foreign ownership that expect foreign companies to invest in companies that are capital and technologically intensive. The proprietary nature of some of the foreign owned assets such as technology and product knowledge may put them in a better position in terms of financial performance as compared to locally owned firms.

From the study it was observed that domestic owned firms have a poorer performance than foreign owned firms. This observation may vindicate proponents of foreign direct investment as being more visionary than those who propose the protection of local resources and industries. It may also buoy foreign companies and make them more assertive in seeking concessions from countries in which they operate by highlighting their superior utilization of resources. While foreign investment may have its economic gains for a country, their sustainability and long-term interest may be counter productive to domestic economies.

5.2 Conclusions

The following conclusions from the study emerge resulting from the data analysis. As one of the objectives was to determine the relationship between ownership and financial performance of firms, the results indicated that there might be a relationship between ownership and financial performance of firms quoted on the NSE.

Empirical evidence from the study indicates that there is a negative relationship between domestic ownership and financial performance of firms quoted on the NSE. The results from the data indicate that as the level of domestic ownership increasers, the financial performance of the firms reduces. This negates the home field advantage hypothesis which proposes that domestic firms should perform as well if not better than foreign owned firms as they understand the local business environment better.

The empirical evidence emerging from the study negates the home field advantage hypothesis of locally owned firms. These firms are expected to post superior results as compared to foreign owned firms as they possess certain advantages emanating from the local environment. Foreign companies are able to surmount the challenges brought about by structural agency costs, culture, language, regulatory issues, distance between the parent firm and their local subsidiaries and monitoring costs. These factors seem not to influence the performance of foreign firms in Kenya.

The study also established that foreign ownership and financial performance of firms on the NSE are positively related. The level of financial performance of foreign owned firms increases as the level of foreign ownership increases. This collaborates the various theories of foreign ownership such as the specific advantage hypothesis, general global advantage hypothesis and limited form of global advantage hypothesis among others.

The study has therefore established empirically that foreign owned firms have superior performance as compared to firms that are domestic owned. The study has also established that there might be a relationship between ownership and financial performance. Conclusively, foreign ownership has a positive impact while domestic ownership has a negative impact on financial performance.

5.3 Policy Recommendations

The findings on the relationship between foreign owned firms and their domestic counterparts and financial performance used to inform policy. It is necessary to note that the results show the average performance but does not rule out stellar performance for some domestic owned firms on their own. As observed by other researchers, it is possible for domestic owned firms to attain the same level of productivity as foreign owned firms with appropriate management. Governments would be erring if they were to adopt the concept that only foreign owned firms may be in a position to efficiently utilize resources and develop pro-foreign firm's investment policies.

Developing countries find themselves in a precarious position, as they need to nurture young and growing firms in their countries while at the same time advocating for worldwide benchmarking. MNE's have a long history of production and are able to exploit economies of scale by adopting the best technologies and investing in R&D. these advantages that foreign firms enjoy can be passed on to domestic owned firms through partnerships with the multinationals. The partnerships could be government driven through provision of subsidies to companies that fully engage with domestic owned firms through partnerships. This may encourage the foreign MNE's to transfer their best practices to domestic economies and enjoy the benefits.

In attracting foreign direct investments, policy makers can stick to areas where foreign firms are reluctant to transfer their proprietory knowledge to domestic owned firms. This is especially so in fields such as emerging technologies and heavy manufacturing. In fields such as services and widely available technology, the policy makers can restrict entry by foreign owned firms as they profer no benefits to the country. The governments can therefore restrict foreign firms to specific sectors of the economy and leave the less competitive to the domestic firms.

5.4 Limitations of the Study

The research study expected to encounter certain obstacles that may have affected the results or outcome of the study. These problems can be controllable while others are uncontrollable. One of the controllable obstacles included wrong computations by the

researcher from the raw data contained in the publications by the companies and the NSE. Double-checking the data collected solved the obstacle before recording it in the computer for analysis.

The researcher may also have carried out wrongful analysis of the data leading to wrong interpretation of the data and therefore wrong conclusions. In order to avoid this limitation, the researcher relied on a statistical package to analyse the data and used the SPSS package version 16 as version 17 was not available. The role of the researcher was to interpret the data as the data analysis was by the computer. The interpretation and conclusions based on computer analysis is likely to be more accurate.

One of the uncontrollable limitations for the study was the reliability of the data used by the researcher. The data obtained from financial statements published by the companies and the NSE has the likelihood of the being a bit subjective, as it is prepared with a certain audience in mind. The data may therefore suffer from window-dressing and creative accounting to please the shareholders. The researcher however had no option but to assume that the reporting entities met the other regulatory bodies such as the CMA and NSE disclosure requirements.

5.5 Suggestions for Further Research

The study established that there might be a relationship between ownership and financial performance. Future researchers may find it interesting to identify the factors that contribute to lower performance as the level of domestic ownership increases as opposed to higher financial performance as the level of foreign ownership increases. These factors responsible for 88% of the variation of financial performance of firms could explain the variability that does not relate to ownership.

Another area of interest to future researchers is the identification of the factors that contribute to poor performance as the domestic ownership of firm's increases. Which of these factors could be responsible for the poor performance? Do domestic firms exploit their home advantage and market knowledge to their advantage? Researchers could be

interested in identifying the challenges that deter domestic owned firms from exploiting these advantages.

Future researchers may also want to identify the specific advantages that foreign firms utilize to overcome new markets especially in developing economies. The researchers may want to identify whether the high financial performance levels associated with foreign ownership of firms replicates in other emerging markets in Africa and the world as a whole.

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Appendix 1

Companies Listed on the NSE by Sector.

Agriculture Sector
Kakuzi Limited
Rea Vipingo Plantations Ltd
Sasini Tea and Coffee Limited 1

Commercial and Services
Accesskenya Group
Car and General (Kenya) Limited
CMC Holdings Limited
Kenya Airways Limited
Nation Media Group Limited
Scangroup Limited
Standard Group Limited
TPS (Tourism Promotion Services) Eastern Africa Limited (Serena Hotels)

Financials and Investments
Barclays Bank of Kenya Limited
CFC Stanbic Bank (Formerly CFC Bank)
Diamond Trust Bank (Kenya) Limited
Equity Bank Limited
Housing Finance Company Limited
Centum Investment Company (ICDCI) Limited
Jubilee Holdings Limited
National Bank of Kenya Limited
Kenya Commercial Bank Limited
Kenya Reinsurance Corporation Ltd
NIC Bank Limited
Olympia Capital Holdings Limited
Pan Africa Insurance Company Limited
Standard Chartered Bank Kenya Limited

Industrial and Allied Sector
Athi River Mining Limited
Bamburi Cement Company Limited
British American Tobacco Kenya Limited
Crown Berger Kenya Limited
East African Cables Limited
East African Portland Cement Company
East African Breweries Limited
Eveready East Africa Limited
Kenya Oil Company Limited
BOC Kenya Limited
The Kenya Power & Lighting Co. Ltd

Kenya Electricity Generating Company (Kengen)
Total Kenya Ltd
Mumias Sugar Company Ltd
Sameer Africa Limited
Unga Group Limited

The Alternative Investment Market Segment (AIMS)
Eaagads Limited
Express Kenya Limited
Kapchorua Tea Company Limited
Williamson Tea Kenya Limited
Limuru Tea Company Limited

Appendix 1I

Companies covered and data used in the analysis

	F Ownership	DOM ownership	Performance
Kakuzi Limited	0.51	0.49	0.21666667
Rea Vipingo Plantations Ltd	0.56	0.44	0.24666667
Sasini Tea and Coffee Limited 1	0.25	0.75	0.12533333
Accesskenya Group	0.37	0.63	0.235
Car and General (Kenya) Limited	0.48	0.52	0.27
CMC Holdings Limited	0.01	0.99	0.22
Kenya Airways Limited	0.385	0.615	0.29666667
Nation Media Group Limited	0.45	0.55	0.39333333
Scangroup Limited	0.51	0.49	0.52666667
Standard Group Limited	0.69	0.31	0.70333333
TPS (Tourism Promotion Services)	0.52	0.48	0.13666667
Barclays Bank of Kenya Limited	0.68	0.32	0.45333333
CFC Stanbic Bank (Formerly CFC Bank)	0.41	0.59	0.20666667
Diamond Trust Bank (Kenya) Limited	0.39	0.61	0.23333333
Equity Bank Limited	0.25	0.75	0.23
Housing Finance Company Limited	0.01	0.99	0.08
Centum Investment Company (ICDCI) Limited	0.01	0.99	0.12333333
Jubilee Holdings Limited	0.44	0.56	0.24
National Bank of Kenya Limited	0.01	0.99	0.29666667
Kenya Commercial Bank Limited	0.12	0.88	0.31
Kenya Reinsurance Corporation Ltd	0.01	0.99	0.175
NIC Bank Limited	0.01	0.99	0.23333333
Olympia Capital Holdings Limited	0.19	0.81	0.13
Pan Africa Insurance Company Limited	0.01	0.99	0.06666667
Standard Chartered Bank Kenya Limited	0.738	0.262	0.46666667
Athi River Mining Limited	0.01	0.99	0.21666667
Bamburi Cement Company Limited	0.716	0.284	0.33
British American Tobacco Kenya Limited	0.68	0.32	0.44333333
Crown Berger Kenya Limited	0.183	0.817	0.12
East African Cables Limited	0.01	0.99	0.51333333
East African Portland Cement Company	0.41	0.59	0.26333333
East African Breweries Limited	0.5	0.5	0.55666667
Eveready East Africa Limited	0.1	0.9	0.33
Kenya Oil Company Limited	0.64	0.36	0.2
BOC Kenya Limited	0.66	0.34	0.25
The Kenya Power & Lighting Co. Ltd	0.01	0.99	0.11666667
Kenya Electricity Generating Company	0.01	0.99	0.06333333

(Kengen)			
Total Kenya Ltd	0.78	0.22	0.17
Mumias Sugar Company Ltd	0.03	0.97	0.23
Sameer Africa Limited	0.16	0.84	0.05
Unga Group Limited	0.025	0.975	0.15666667
Eaagads Limited	0.82	0.18	0.08666667
Express Kenya Limited	0.6	0.4	0.12666667
Kapchorua Tea Company Limited	0.27	0.73	-0.0633333
Williamson Tea Kenya Limited	0.56	0.44	0.02
Limuru Tea Company Limited	0.52	0.48	0.21