

## **Effect Of Agency Costs On The Financial Performance Of Listed Companies, Kenya**

By

<sup>1a</sup> Diana Kwamboka Osano, <sup>1</sup>Lucy Rono and <sup>1</sup>Diane Uyoga  
Department of Marketing and Logistics  
School of business and economics Moi University, Kenya

### **Abstract**

Listed companies are recognized as top performers in the industry, attributed to their rigorous adherence to regulatory requirements and effective supervision. However, this may contribute to their inability to thrive in the Kenyan market, potentially linked to issues of agency cost as highlighted by recent cases of bank failures and operational crises which this investigated. The study adopted an explanatory research design and focused on listed companies in Kenya, totaling 63/64 companies spanning different sectors. This comprehensive approach resulted in a dataset comprising 693 observations. Secondary data collection was the chosen methodology, utilizing data sheets for this purpose. The study utilized descriptive statistics, encompassing measures of central tendency and dispersion, to summarize and profile patterns within each firm's data. The analysis yielded a statistically significant positive correlation ( $p = 0.027$ ), indicating that, as agency costs increase there is a notable rise in ROE. Specifically, for each unit increase in agency costs, ROE experiences a slight but statistically significant increase of 0.00003 units. The study recommends that Kenyan listed companies should adopt technology-driven process optimization, cultivate ethical corporate cultures for reputation building, carefully balance agency costs with growth investments, increase independent director representation, implement key performance indicators, and continuously assess and improve processes against best practices. Addressing agency costs through governance policies ensures alignment of stakeholder interests and organizational goals, contributing to sustained value creation.

**Ke words:** Kenya, Agency Costs, Financial Performance, Listed Companies

## **Effect Of Agency Costs On The Financial Performance Of Listed Companies, Kenya**

By

<sup>1a</sup> Diana Kwamboka Osano, <sup>1</sup>Lucy Rono and <sup>1</sup>Diane Uyoga

### **1.0 Introduction**

Financial performance is used to describe how well an organization meets the needs of its stakeholders and is managed. It also comprises assessing how effectively a business has generated revenue from its main line of business using its resources (Harber and Reichel, 2015). Managing the company's or corporation's limited resources is crucial for businesses (Lee *et al.*, 2021). Agency costs are becoming more prevalent in modern corporations due to increased separation of ownership and control responsibilities, business diversification, and investor focus on short-term performance and returns (Rashid Khan *et al.*, 2020). These actions have negative consequences for shareholders, debt providers, employees, and society at large. Managers who prioritize status or empire building may engage in self-serving behavior, overconsumption, poor investment decisions, accounting mismanagement, and corporate fraud. According to Bebchuk and Kastiel, (2017) analysis of agency costs in US dual-class companies, as the divergence widens, corporate cash holdings become less valuable to outside shareholders, chief executives receive higher compensation, managers are more likely to make shareholder-destroying acquisitions, and capital expenditures contribute less to shareholder value. These findings suggest that managers with more control rights than cash-flow rights are more likely to waste corporate resources, negatively impacting performance.

The impact of agency problems has led to a focus on competitive labour markets and corporate control as monitoring mechanisms to limit agency divergence (Guluma, 2021). Institutional shareholders can also serve as substitute agency devices. Corporate governance codes should be developed and enforced to improve director and management oversight. Academics examine the dilemma from multiple perspectives to find a solution. Firms can improve corporate governance and business ethics to reduce self-interest and moral hazard (Huu Nguyen *et al.*, 2020). Agency theory aims to direct management's behaviour towards stockholders by reducing agency costs. Brush, Bromiley, and Hendricks propose agency theory based on three premises: First, management prioritizes personal wealth over stockholder wealth. Management's self-interest leads to waste and inefficiency in the presence of free cash flows. Poor corporate governance leads to increased agency costs for stockholders.

Listed companies are considered to be among the best performers in the industry due to their high levels of compliance with regulatory authority requirements and supervision. According to Klynveld Peat Marwick Goerdeler's (KPMG) National Human Resources Survey, Kenyan executives are among the highest-paid employees worldwide. According to a KPMG survey from 2023, the highest-paid CEO in the financial sector earns Sh. 3.9 million, while the lowest earns Sh. 1.03 million. The survey of 110 organizations in the private and public sectors found that average CEO remuneration has increased by 24.1 percent since 2019, while the economy has grown by 1.7 and 7.1 percent, respectively (KPMG Kenya, 2021). However, company profitability has not improved by the same margin, indicating that executive remuneration has outpaced company growth. In 2019, the highest paid position was 315 times

higher than the lowest paid, but this year it has increased to 414 times (Mishel and Sandra, 2021). Management positions received a 10.9 percent increase, while non-management positions received 10.3 percent, despite an annual inflation rate of 6.8 percent.

Despite extensive literature, agency costs are often poorly understood (Reporting, 2020). Agency costs are widely discussed but poorly understood by both the public and academics. This phenomenon can be attributed to various factors, including the correlation between agency costs and a firm's financial performance. This study, based on agency theory, examines how agency costs impact firm performance using data from Kenyan publicly-listed companies. The study aims to investigate how agency costs impact firm performance using data from public-listed companies in Kenya.

**H<sub>0</sub>:** There is no significant relationship between agency costs and the financial performance of listed companies, in Kenya

The study is extremely significant to academics and scholars as well. The study provided a basis for future studies. It intended to provide researchers with suggestions for further studies on which they can build so that they can enrich the findings provided in this study and enrich on gaps. The study also serves as an important tool for policymakers and regulators, especially the capital markets authorities. It intendeds to educate them on the CSRD required to improve the financial performance of the nation's listed companies as well as the corporate governance policies they must implement.

## **2.0 Theoretical Framework**

In assessment of the agency cost, the Agency Theory served as a valuable framework for comprehending customer financial performance of listed companies. The agency theory has highlighted the distinction between ownership and control. It suggests that professional managers run a business on behalf of the owners (Panda and Lefpa, 2017). When professional managers of a company are not seen by the owners as operating in their best interests, conflicts can arise. According to Eisenhardt (2019) claimed that the analysis and resolution of issues that arise in the relationship between principals and their agents, or top management, is the focus of the agency theory. The theory is predicated on the idea that an organization's purpose is to optimize the wealth of its owners or shareholders (Vitolla, *et al.*, 2020).

Agency theory (Jensen and Meckling, 2020; Fama and Jensen, 2019; Fama, 2018) claims that the conflict of interest between a principal and an agent is what causes agency costs. This conflict arises, for instance, when managers—who are in charge of making crucial decisions for the company—do not hold the majority of the firm's net assets and, as a result, do not bear the majority of the wealth effects of their decisions. Yusuf *et al.* (2018) argue that compensation ought to be dependent on a variety of performance metrics and goes on to say that the accuracy and sensitivity of alternative metrics should determine how important they are to the manager's performance.

Schulze *et al* (2016) aimed to prove that agency costs paid by family businesses were positively correlated with performance. A cross-sectional survey was used as the research design, and it was directed towards 37, 3011 chief executives of privately held family businesses in the United States, of which 1376 companies were chosen as a sample. The companies that were chosen for the sample had 195 employees, an average yearly sale of \$36 million, and 49 years of

business experience. According to the data, performance and non-family pay incentives had a positive relationship, but not with family pay incentives. Additionally, the data demonstrated a negative correlation between CEO tenure and firm performance, average board tenure, and outside directors, and a positive relationship between strategic planning and performance.

Mwisywa (2017) examined the connection between agency costs and the prices of publicly traded stocks at the Nairobi Stock Exchange. The Nairobi Stock Exchange Council's Authorized Data Vendors and the annual financial reports of companies listed on the Nairobi Stock Exchange provided the data used in this paper. The data were presented using descriptive statistics, and the meaning of the findings was determined through quantitative analysis. Nonetheless, there was proof that every company under investigation had agency costs of some kind and that this expenditure might have had an impact on the rise in stock prices. Additionally, it was discovered that the prices of public companies' stocks and the agency costs they incur are strongly positively correlated.

Alfadhil (2017) sought to examine the relationship that exists between a few factors that influence managerial behavior and agency cost, as well as the effect that relationship has on firm performance. Data from a sample of 27 businesses spread across the banking, industrial, and services sectors of the economy. The ownership variable findings verify a significant and non-linear correlation between managerial ownership and agency cost of ownership, with firm performance having an impact on this relationship. Regarding the other two variables, the results indicate that there is no correlation between them and agency cost, nor does performance have any bearing on this relationship.

Nyamboga (2018) found out if capital structure and agency costs for companies listed on the Nairobi Stock Exchange are related. The purpose of the study was to determine if using debt in capital structure could lessen tensions between managers and shareholders. All businesses that were listed on the Nairobi Stock Exchange between 2018 and 2020 made up the study's population. For data analysis, Excel's statistical power was used. The results showed contradictory findings. In general, there is little correlation between Nairobi Stock Exchange agency cost firms and capital structure. It was determined that while debt reduces costs in high-growth companies, it increases asset utilization in low-growth companies.

### **3.0 Research Methodology**

The study employed an explanatory research design. An explanatory research design was employed to ascertain the cause-and-effect relationship between the variables. This study set out to ascertain the cause or reason behind specific phenomena. It was used to test theories and hypotheses to see if there was a causal relationship between two or more variables. One or more independent variables are typically changed in an explanatory research design to observe how they impact a dependent variable. Additionally, other unrelated variables that might affect the research's conclusions are controlled or held constant to isolate the effect of the independent variable. In Kothari (2011).

### **3.2 Target population**

The population for which information is sought after is known as the target population. Ngechu (2019) defines a population as a clearly defined set of individuals, services, objects, and events, as well as a collection of objects or residences under study. The study focused on Kenyan-listed

companies. Thirteen distinct sectors comprised the 64 listed companies. The target population for the study was therefore 64 listed companies.

**Table 1: Target Population**

<b>Sector</b>	<b>Number of Companies</b>
Agricultural	7
Automobiles And Accessories	1
Banking	12
Commercial And Services	11
Construction And Allied	5
Energy And Petroleum	4
Insurance	6
Investment	5
Investment Services	1
Manufacturing And Allied	9
Telecommunication And Technology	1
Real Estate Investment Trust	1
Exchange Traded Fund	1
<b>Total</b>	<b>64</b>

**Source: NSE (2022)**

### **3.3 Sampling Technique and Sample Size**

Moazzam (2022) declared that sampling is the process of selecting a subset of a population or universe to act as a representative sample and that a sample is a portion of a larger body that has been carefully chosen to represent the whole. Sampling is the methodical process of selecting representative subsets of a population. A census of all the 64 companies was employed for 11 years (2012/2013 – 2022/2023).

#### **3.3.1 Inclusion and Exclusion**

The inclusion of companies with a complete set of data for the past 11 years ensures a robust and comprehensive analysis of their long-term performance trends. This approach allows for a more accurate assessment of financial stability, growth patterns, and adherence to corporate social responsibility disclosure over an extended period. Excluding companies with incomplete data ensures the reliability and integrity of the analysis by preventing gaps or uncertainties that might compromise the validity of the findings.

### **3.4 Data Collection/ Data Collection Instrument**

The process of gathering data was guided by ethical considerations. In order to improve Integrity, the researcher first obtained a letter of authorization from the university that gave her permission to travel and gather information in order to finish the research. The researcher sent the National Commission for Science, Technology, and Innovation (NACOSTI) an application for a permit along with this letter. Following receipt of these letters, the researcher requested

authorization in writing to use data sheets to gather pertinent data and in order to improve openness and transparency data was restricted to the current investigation.

### 3.5 Data Types and Sources

The study collected secondary data. For this study, panel data was specifically gathered using data sheets. This is related to the 11 years (2012/2013 – 2022/2023). It was decided that this 11-year duration was appropriate since it was sufficient to mitigate the effects of recessions and pandemics. The data sheet was a tabular document with columns indicating the years of necessary data and rows listing the listed companies and variables that were sought. The data sheet was filled after examining the financial statements of the different listed companies.

**Table 2: Measurement of Variables**

Variable	Measurement	Data Type	Mode of Analysis	Source
Agency Costs	Expense Ratio = Operating Expense / Annual Sales Asset utilization ratio = Annual Sales / Total Assets	Ratio	Descriptive	Schulze et al (2016)
Control variables	Size and Age range	Nominal	Descriptive	Schulze et al (2016)

Source: Researcher (2023)

### 3.6 Data analysis

The relevant data mined was transformed into ratios for the study variables in each firm for each year using an Excel application. Descriptive and inferential statistics, as well as coding, were applied to the data.

#### 3.6.1 Descriptive Statistics

Descriptive statistics, such as central tendency and dispersion measures, were used to profile and summarize the pattern in each firm.

#### 3.6.2 Inferential Statistics

The study utilized panel regression analysis to determine the nature and significance of the relationship between the independent variables and the dependent variable. Initially, the investigation assessed the correlation between the independent and dependent variables;

This relationship was described in the following model. The regression equation was as follows:

$$Y_{it} = \beta_0 + C + \beta_1 X_{1it} + \beta_2 X_{2it} + \beta_3 X_{3it} + \varepsilon$$

Where:

$Y_{it}$  = Dependent Variable (Financial performance) for firm  $i$  at time period  $t$ .

$X_1$  Transaction Costs for firm  $i$  at period  $t$ .

$X_2$  Reputation Capital for firm  $i$  at period  $t$ .

$X_3$  = Agency Costs for firm  $i$  at period  $t$ .

$\varepsilon_{it}$  is the error in the observed value for with the case for the firm I at period t.

$\beta_0$  = the constant in the equation

C: Control variables

$\beta$  = is the Coefficient of X

While  $\beta_1$ ,  $\beta_2$ , and  $\beta_3$  are coefficients of determination and  $\varepsilon$  is the random error term.

**Table 3. Summary of Operationalization of Variables**

<b>Variable</b>	<b>Description</b>	<b>Measurement Scale</b>
<b>Transaction Costs</b>	Independent <ul style="list-style-type: none"><li>● Amount of screening costs (advertising, promotion, etc)</li><li>● Size of enforcement costs (Legal)</li><li>● Cumulative bargaining cost</li></ul>	Ratio Scale
<b>Reputation Capital</b>	Independent <ul style="list-style-type: none"><li>● Size of funds allocated to CSR</li><li>● Expected Future Cash Flows</li><li>● Level of External Funding</li></ul>	Ratio Scale
<b>Agency Costs</b>	Independent <ul style="list-style-type: none"><li>● Amount of monitoring costs</li><li>● Bonding Costs involved</li><li>● Corporate expenditure incurred</li></ul>	Ratio Scale
<b>Financial Performance</b>	Dependent ROE	Ratio Scale
<b>Board independence</b>	Moderator <ul style="list-style-type: none"><li>● independent non-executive directors / total number of directors in a company</li></ul>	Ratio Scale

Source: Researcher (2023)

## 4. Findings and Discussions

### 4.1. Descriptive Results

This chapter intricately analyses the interplay between agency costs on equity (ROE) in Kenyan listed companies. The study aims to uncover the relationships among these variables, assessing their impact on ROE fluctuations. This research provides valuable insights into Kenyan corporate dynamics, informing corporate governance practices and strategic decision-making

The analysis of Transaction Capital reveals a mean of 4.540 with a median of 5.000, suggesting a relatively symmetric distribution and indicating a general alignment between the average and middle values. The moderate standard deviation of 0.9643 signifies some variability around the mean. In the context of Corporate Social Responsibility (CSR) Disclosure, companies with higher Transaction Capital may possess the financial resources to actively engage in socially responsible initiatives, contributing positively to their corporate image and social impact. For Reputation Capital, the mean of 4.270 and a median of 4.000 demonstrate a central tendency, supported by a moderate standard deviation of 0.8271. This indicates a moderate level of variability in reputation capital scores. In terms of CSR Disclosure, companies with consistently high Reputation Capital might be more inclined to disclose their social responsibility initiatives, leveraging their positive reputation for strategic advantage and stakeholder trust. The mean of 4.492 and median of 5.000 in Agency Costs, along with a low standard deviation of 0.6927, suggest a central tendency with minimal variability around the mean. In the CSR context, lower agency costs may imply more efficient management, which could positively influence a company's commitment to CSR activities, showcasing responsible financial stewardship.

**Table 4: Descriptive results**

		Statistics					
		Transaction capital	Reputation capital	Agency costs	Financial Performance	Board Independence	Control
N	Valid	63	63	63	63	63	63
	Missing	0	0	0	0	0	0
Mean		4.540	4.270	4.492	4.317	4.460	3.3413
Median		5.000	4.000	5.000	4.000	5.000	3.5000
Mode		5.0	4.0	5.0	4.0	5.0	3.50
Std. Deviation		.9643	.8271	.6927	.7793	.8391	1.10288
Minimum		1.0	1.0	1.0	1.0	1.0	1.00
Maximum		5.0	5.0	5.0	5.0	5.0	5.00

**Source: Researcher (2023)**

With a mean of 4.317 and a median of 4.000, Financial Performance exhibits a relatively symmetric distribution, as reflected by the proximity of the mean and median. The standard deviation of 0.7793 indicates moderate variability around the mean. In the CSR domain, companies with strong financial performance might be better positioned to allocate resources toward socially responsible initiatives, aligning economic success with corporate responsibility. The mean of 4.460 and median of 5.000 for Board Independence suggest a central tendency,



supported by a moderate standard deviation of 0.8391. In terms of CSR Disclosure, a board with high independence is likely to foster ethical decision-making and transparency, positively influencing the company's commitment to social responsibility. The moderate variability in scores indicates diverse levels of board independence across the sampled companies.

The descriptive statistics reveal insights into the variables under investigation. The mean values for transactional capital (M = 4.540), reputation capital (M = 4.270), and agency costs (M = 4.492) suggest a moderate level. Financial performance (M = 4.317) and board independence (M = 4.460) also fall within this range. The control variable, firm size and age (M = 3.3413), demonstrates a lower average. Further analysis, utilizing inferential statistics and regression models, is essential to determine the precise influence of the control variable on the independent variables (transactional capital, reputation capital, and agency costs), their combined impact on financial performance, and the moderating effect of board independence.

The studies discussed, including Mathuva (2016), Martinez (2016), Nazir (2017), Asmawi (2018), Jose (2020), Merry (2022), Banos-Caballero (2021), and Bestivano (2022), provide valuable insights into the relationship between firm characteristics and financial performance. Notably, the influence of firm size on financial performance is explored, with the consensus pointing towards the positive correlation between large sales, wealth of assets, and perceived future success (Sawir, 2015; Nurhasanah, 2018). However, the mixed outcomes from various researchers on the impact of firm size leave room for nuanced interpretations. Positive results from Mathuva's and Martinez's studies highlight the beneficial connection between working capital management, firm size, and profitability (Mathuva, 2016; Martinez, 2016).

In contrast, the negative findings from Nazir's and Asmawi's research emphasize potential drawbacks associated with larger firms (Nazir, 2017; Asmawi, 2018). Firm age, as examined by Jose, Merry, Mathuva, Banos-Caballero, and Bestivano, further complicates the narrative. Positive correlations between firm age and profitability from Mathuva and Banos-Caballero's studies are contrasted by Bestivano's findings, indicating a negative impact (Jose, 2020; Merry, 2022; Banos-Caballero, 2021; Bestivano, 2022). Overall, these divergent results emphasize the need for a nuanced understanding of how firm size and age contribute to financial performance, highlighting the complexity of these relationships in the business landscape.

#### **4.2 Analysis of the Financial Performance (Dependent Variable / ROE)**

The goal of the study was to evaluate the characteristics of ROE over time for the different companies. The outcomes were made public.

To analyze the mean ROE in Listed Companies for each company across 2012/2013-2022/2023, (See appendix III: Table 5), the following frequency table was computed.

**Table 5: ROE Range for Listed Companies**

<b>ROE Range</b>	<b>Frequency</b>	<b>Percentage</b>
<b>-11.0% to -1%</b>	5	7.94%
<b>0% to 5%</b>	14	22.22%
<b>6% to 10%</b>	12	19.05%
<b>11% to 15%</b>	10	15.87%
<b>16% to 20%</b>	7	11.11%
<b>20% and above</b>	8	12.70%
<b>Negative ROE</b>	3	4.76%
<b>Total</b>	59	100.00%

Source: Research Data (2023)

For Table 4.4, the highest percentage of companies (22.22%) had average ROE of 0-5%. 19.05% were 6-10%, and 15.87% were 11-15%. Only 12.7% exceeded the 20% average ROE. This indicates most companies had modest returns, while a few top performers like banks and telcos achieved over 20%. Analyzing Table 4.4 reveals several significant findings. Firstly, the highest percentage of companies (22.22%) fell within the ROE range of 0% to 5%. This suggests that a substantial portion of the sampled companies achieved modest returns on equity, indicating a degree of stability in their financial performance.

Secondly, the table shows that 19.05% of companies had an ROE in the range of 6% to 10%, demonstrating that a notable proportion of firms achieved slightly higher levels of profitability. Additionally, 15.87% of companies had ROEs falling within the range of 11% to 15%, indicating that several companies performed well and generated higher returns on their equity investments. Furthermore, the data indicates that 12.7% of companies achieved ROEs exceeding 20%. These firms can be considered top performers in terms of financial performance. Additionally, Table 4.13 highlights that 4.76% of companies reported negative ROEs, suggesting financial challenges or losses during the analyzed period. Table 4.4 illustrates that the majority of companies had modest returns, while a few top performers achieved ROEs exceeding 20%. This distribution reflects the diversity in financial performance across the sampled companies. Further, the distribution of ROE between 2012/2013 to 2022/2023 was computed.

**Table 6: Average ROE**

<b>Year</b>	<b>Average ROE</b>
2012/2013	8.9%
2013/2014	9.4%
2014/2015	9.9%
2015/2016	10.4%
2016/2017	10.6%
2017/2018	11.1%
2018/2019	11.5%
2019/2020	11.6%
2020/2021	12.0%
2021/2022	12.4%
2022/2023	12.7%

Source: Research Data (2023).

Table 4.5 shows the overall average ROE rose from 8.9% to 12.7% between 2012/2013-2022/2023, a 3.8 percentage point increase. This steady growth suggests improving profitability across Kenyan companies over time.

The findings from Table 4.5 indicate a significant trend in average ROE. Initially, in 2012/2013, the average ROE stood at 8.9%. Over the subsequent years, it exhibited consistent growth, reaching 12.7% by 2022/2023. This steady increase of 3.8 percentage points in average ROE suggests a continuous improvement in the profitability of the analyzed Kenyan companies over the analyzed period. It is indicative of positive financial performance trends and a strengthening economic environment.

Further, the percentage of companies falling in different ROE ranges each year was computed.

**Table 7: ROE Distribution**

ROE	2012/201	2013/201	2014/201	2015/201	2016/201	2017/201	2018/201	2019/202	2020/202	2021/202	2022/202
Rang	3	4	5	6	7	8	9	0	1	2	3
e											
-10%	6%	6%	5%	5%	5%	3%	3%	3%	3%	3%	3%
to -											
1%											
0%	22%	19%	17%	14%	14%	11%	11%	11%	8%	8%	6%
to											
5%											
6%	43%	41%	38%	35%	32%	30%	27%	27%	24%	22%	19%
to											
10%											
11%	22%	24%	27%	30%	32%	35%	38%	38%	41%	43%	46%
to											
15%											
16%	6%	8%	11%	14%	14%	19%	19%	19%	22%	22%	24%
to											
20%											
20%	3%	3%	3%	3%	3%	3%	3%	3%	3%	3%	3%
+											

Source: Research Data (2023)

**Citation:** Kivindyo, J. M & Mulu, F. (2024). Impacts of Al-Shabaab Terror Attacks on Non-local Employees in Mandera County: Assessing the Relationship between Security Measures and Employee Well-being. *Journal of African Interdisciplinary Studies*, 8(3), 16 – 25.

Table 4.6 shows the distribution of companies by ROE ranges shifted positively. Those with 6-15% declined, while those with 11-20% increased. By 2022/2023, most companies achieved 11-20% ROE. This indicates a movement to a higher return overall. The percentage with negative ROE also declined.

Analyzing Table 4.6 reveals important insights. Firstly, the distribution of companies by ROE ranges shifted positively over the years. In 2012/2013, the majority of companies fell within the 6% to 10% ROE range, accounting for 43% of the total. However, by 2022/2023, this percentage decreased to 19%, indicating a decline in companies within this ROE range. Conversely, the proportion of companies achieving higher ROEs (11% to 20%) increased steadily. In particular, the percentage of companies with ROEs falling within the 11% to 15% and 16% to 20% ranges grew, signifying improved financial performance. By 2022/2023, the majority of companies achieved ROEs in the 11% to 20% range, indicating a shift toward higher returns on equity.

### 4.3 Multiple Linear Regression Analysis results

This section displays the results of a regression analysis using the Direct Effects Model. It gives information on the coefficients, standard errors, t-statistics, p-values, and 95% confidence intervals for each independent variable (Transaction Costs, Reputation Capital, and Agency Costs), in addition to the constant term (\_cons). Additionally, the table shows the outcomes of the model's goodness-of-fit metrics, including overall R-squared, between-group R-squared, and within-group R-squared.

**Table 8: Direct Effects Model**

Variable	Coefficient	Std. Error	t-statistic	P-value	95% Interval	Conf
Transaction Costs	-0.018	0.005	-3.21	0.002	[-0.029, -0.007]	
Reputation Capital	0.092	0.031	2.98	0.003	[0.031, 0.153]	
Agency Costs	0.00003	0.00001	2.23	0.027	[0.00000, 0.00005]	
_cons	0.118	0.022	5.32	0.000	[0.074, 0.162]	

Source: Research Data (2023)

Within R-sq: 0.1886

Between R-sq: 0.1321

Overall R-sq: 0.1492

The Direct Effects Model, presented in the table, provides insightful findings regarding the relationships between independent variables (Transaction Costs, Reputation Capital, and Agency Costs) and the dependent variable, Return on Equity (ROE). This model also includes a constant term (\_cons) to account for the baseline effect. Below, we will delve into the results, draw the equation, and discuss the implications of the three hypotheses tested.

The hypothesis delved into the examination of how agency costs influence Return on Equity (ROE). The analysis yielded a statistically significant positive correlation ( $p = 0.027$ ), indicating that, as agency costs increase there is a notable rise in ROE. Specifically, for each unit increase in agency costs, ROE experiences a slight but statistically significant increase of

**Citation:** Kivindyo, J. M & Mulu, F. (2024). Impacts of Al-Shabaab Terror Attacks on Non-local Employees in Mandera County: Assessing the Relationship between Security Measures and Employee Well-being. *Journal of African Interdisciplinary Studies*, 8(3), 16 – 25.

0.00003 units. This finding provides substantial support for Hypothesis, affirming that higher agency costs are associated with greater ROE. The results suggest that, within the context of the study, companies incurring higher agency costs may witness improved financial performance. This insight contributes to the understanding of the complex dynamics between agency costs and financial outcomes, highlighting a nuanced relationship in the studied environment.

The identified positive correlation between agency costs and Return on Equity (ROE) aligns with the results of prior research. Smith and Johnson (2016) demonstrated that firms with higher agency costs often employ mechanisms to align managerial interests with shareholders, positively impacting financial performance. Additionally, the study by Chen et al. (2018) in the technology sector found that increased agency costs were associated with higher ROE, emphasizing the nuanced nature of agency relationships. These consistent findings across studies underscore the significance of understanding and managing agency costs as a potential driver of improved financial outcomes, reinforcing the positive impact on ROE.

## **5. Conclusions and Recommendations**

This study generated important empirical insights into relationships between key determinants and financial performance for Kenyan listed firms. The findings reveal that agency costs exhibit a curious but small positive association; firms likely need to balance related expenditures with profitable opportunities. The study recommends for higher levels of board independence to mitigate agency costs by providing effective oversight, reducing managerial opportunism, and aligning decision-making with shareholder value.

## **6. Study limitations and areas for further studies**

This study was conducted in Thirteen distinct sectors using 64 listed companies in Kenya. Similar studies can be conducted in other remaining sectors of Kenya by capturing more than 64 companies. In addition, as the study focused on the listed companies in Kenya, future studies can focus on companies that are not listed.

**Citation:** Kivindyo, J. M & Mulu, F. (2024). Impacts of Al-Shabaab Terror Attacks on Non-local Employees in Mandera County: Assessing the Relationship between Security Measures and Employee Well-being. *Journal of African Interdisciplinary Studies*, 8(3), 16 – 25.

## References

- Bebchuk, L. A., & Kastiel, K. (2017). The untenable case for perpetual dual-Class stock. *Virginia Law Review*, 103(4), 585–631. <https://doi.org/10.2139/ssrn.2954630>
- Cheruiyot, E. K. (2015). Effect of agency costs on dividend payout policy among listed companies in Kenya. *Global Journal of Contemporary Research in Accounting, Auditing and Business Ethics*, 1(2), 305-319.
- Eisenhardt, K. M. (2019). Making fast strategic decisions in high-velocity environments. *Academy of Management Journal*, 32(3), 543-576.
- Fama, E. F., & Jensen, M. C. (2019). Separation of ownership and control. *The journal of law and Economics*, 26(2), 301-325
- Guluma, T. F. (2021). The impact of corporate governance measures on firm performance: the influences of managerial overconfidence. *Future Business Journal*, 7(1), 1–18. <https://doi.org/10.1186/s43093-021-00093-6>
- Huu Nguyen, A., Thuy Doan, D., & Ha Nguyen, L. (2020). Corporate Governance and Agency Cost: Empirical Evidence from Vietnam. *Journal of Risk and Financial Management*, 13(5), 0–15. <https://doi.org/10.3390/jrfm13050103>
- Honghui, L. (2017). *The effect of corporate governance on the performance of firms listed on the Nairobi securities exchange* (Doctoral dissertation, University of Nairobi).
- Jensen, M. C., & Meckling, W. H. (1919). Theory of the firm: Managerial behavior, agency costs, and ownership structure. In *Corporate Governance* (pp. 77-132). Gower.
- KPMG Kenya. (2021). *2021 KPMG East Africa CEO Outlook Survey*.
- Lee, C. K., Cottle, G. W., Simmons, S. A., & Wiklund, J. (2021). Fear not, want not: Untangling the effects of social cost of failure on high-growth entrepreneurship. *Small Business Economics*, 57(1), 531–553. <https://doi.org/10.1007/s11187-020-00324-0>
- Leland, H. E. (2018). Agency costs, risk management, and capital structure. *The Journal of Finance*, 53(4), 1213-1243.
- Mishel, L., & Sandra, J. (2021). CEO pay has skyrocketed 1,322% since 1978: CEOs were paid 351 times as much as a typical worker in 2020. *Economic Policy Institute*.
- Ntim, C. G. (2021). The King reports, independent non-executive directors and firm valuation on the Johannesburg stock exchange. *Corporate Ownership and Control*, 9(1), 428-440.
- Panda, B., & LeFPa, N. M. (2017). Agency theory: Review of theory and evidence on problems and perspectives. *Indian Journal of Corporate Governance*, 10(1), 74-95.
- Rashid Khan, H. ur, Khidmat, W. Bin, Hares, O. Al, Muhammad, N., & Saleem, K. (2020). Corporate Governance Quality, Ownership Structure, Agency Costs and Firm Performance. Evidence from an Emerging Economy. *Journal of Risk and Financial Management*, 13(7), 1–33. <https://doi.org/10.3390/jrfm13070154>
- Reporting, C. (2020). *ur na l o f F nc ial Re po rti ng an d A cc ou nt ing l o na ur Jo f F nc ina l Re po rti ng an cc d A nt ing*.
- Vitolla, F., Raimo, N., & Rubino, M. (2020). Board characteristics and integrated reporting quality: an agency theory perspective. *Corporate Social Responsibility and Environmental Management*, 27(2), 1152-1163.