ABSTRACT

Corporate governance can be linked to performance of banks due to non-performing asset portfolios (NPAs) in Kenya but this has not been determined empirically. Information is lacking on effect of corporate governance on total income, liquidity and profitability due to NPAs. The purpose of the study was to determine effect of corporate governance on performance of banks due to NPAs in Kenya. The study sought factors contributing to poor performance of banks, effect of corporate governance on total income due to NPAs, effect of corporate governance on liquidity due to NPAs and effect of corporate governance on profitability due to NPAs. The study was guided by a Shareholder theory where the independent variable is corporate governance and dependent variable is performance of banks. The study employed Panel Least square data analysis. Target population was 43 heads of credit of banks operating in Kenya from 2005 to 2012. Simple random sampling technique was used to select a sample size of 24 heads of credit. Secondary data was collected through review of records, reports, journals and books. Primary data was obtained from respondents through questionnaire and interview schedule. Instrument reliability stood at Cronbach's Alpha of 0.65. Objective one was analyzed using percentages and frequencies. Objectives two to four were analyzed using panel data analysis. Poor lending, mismanagement, customers' unwillingness to repay and all the three jointly, contribute to NPAs at 41.7%, 12.5%, 16.7% and 29.2% respectively. Results for objective two showed $a_{1,}$ a_2 and a_3 as 18.525(p=0.065), 85.921(p=0.001) and 45.605(p=0.097) respectively. Hence a unit change in standard deviation in efficiency causes 45.605 standard deviations in total income, significantly. Results for objective three showed $a_{1,}$ a_2 and a_3 as -0.055(p=0.121), 0.363(p=0.000) and -0.101(p=0.292) respectively. Thus a unit change in standard deviation in capital adequacy causes 0.363 standard deviations in liquidity, significantly. Results for objective four showed $a_{1,}$ a_2 and a_3 as 1.463(p=0.704), 36.334(p=0.000) and -9.814(p=0.352) respectively. Hence a unit change in standard deviation in asset quality causes 1.463 standard deviations in profitability significantly. R-Square results were 0.63, 0.665 and 0.161 for profitability, total income and liquidity models respectively. This implies the models are stable and valid for prediction at 63%, 66.5% and 16.1% respectively. In conclusion different factors contribute to NPAs at different levels, corporate governance significantly affect total income, have mixed effect on liquidity and significantly affect profitability. Asset quality and capital adequacy should be carefully evaluated and efficiency enhanced. The study will be significant in the management of financial institutions. Policy makers and regulators may use it. It can also form a basis for further research.