Ownership Concentration, Capital Structure and Stock Returns of Firms Listed at the Nairobi Securities Exchange

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ABSTRACT

Ownership concentration enables majority shareholders to influence the capital structure; a key financing decision that is independently linked to firm performance. Ideally, firm managers should strive to maximize stock returns by selecting an appropriate optimal capital composition that maximizes the trade-off between the cost of leverage and gains. However, the performance benefits are not always realized because the controlling shareholders may adversely affect stock returns by extracting private benefits at the expense of the minority shareholders, leading potential investors to consider the firm as a risky and unattractive investment, hence lowering stock demand and price. This research sought to determine the intervening effect of capital structure on the ownership concentration and stock returns relationship. A census survey was done on sixty-seven firms listed at NSE from 2006 to 2019 and data was obtained from sixty firms that had been listed for at least two years. A fixed effects model was then utilized to conduct data analysis. The four-step mediation process showed that capital structure mediated the connection between ownership concentration and stock returns. The results contribute to the empirical literature by reducing the conflicting positions on the link between ownership concentration and stock returns by introducing capital structure into the relationship and confirming the role of capital structure in performance management. The study recommends that agents be given incentives through monitoring and regulation to ensure that management interests and those of their principals are aligned when important financing decisions are being made to serve the interests of both majority and minority shareholders. This will promote and enhance corporate performance and increase stock returns.

Keywords: Capital Structure, Ownership Concentration, Panel Fixed Effects Model, Stock Returns.

I. INTRODUCTION

A. Background

Ownership concentration (OC) is a situation where ownership and control are separated by having shareholders who own a Proportionate share of the company (Berle & Means, 1932). This control is exercised by having a majority share which gives the majority shareholder the power to vote to influence the outcome of the various decisions of the company. Ownership concentration is also defined as a situation in which more control is given to one or a few dominant owners (Gaur et al., 2015). Ownership concentration gives the shareholder the ability to control the firm's important decisions through the crucial role of monitoring and supervising management interests. The effectiveness of monitoring brings about the alignment effect and managers are forced to pursue profit maximization which results in to increase in stock performance. Malietso (2017) showed that concentrated ownership may improve the performance of a firm by increasing monitoring and alleviating possibilities of hostile takeovers.

However, with high ownership majority shareholders become entrenched, transfer resources to other firms that they control, and deny their minority counterparts the right to receive dividends through their voting power. The entrenchment effects are associated with increased information asymmetries and increased debt as majority owners avoid dilution of their equity, causing investors to consider the firm a risky investment, thus leading to volatility in stock performance (Wang & Shailer, 2015). With an increase in ownership concentration, it is expected that majority owners will influence debt to capital ratio, with a preference for a high debt-to-capital ratio aimed at increasing leverage and preventing managerial opportunism, leading to positive stock performance. Higher debt reduces the cost of funds due to the interest tax shield and hence highly geared firms experience lower costs of funds and higher expected stock returns (Wakaisuka, 2017). However, the increased leverage poses bankruptcy risks, financial distress, and financial risk, hence reducing the attractiveness of the stock and lowering stock performance (Zhang, 2018). Ownership concentration has been measured in previous studies as
percentage of shares possessed by the major stockholder and the proportion of stocks held by the five largest shareholders (Sousa & Galdi, 2016; Narrang, 2018; Madhani, 2016). Other researchers used the Herfindahl-Hirschman Index (HHI) which measures the equity stake of the largest shareholder. HHI provides concentration measures for the whole company but does not effectively clarify the qualified power of the single shareholder; making it unsuitable for analysing the relationship on principal-principal shareholder conflict. This study operationalized ownership concentration through the percentage of shares held by the five largest stockholders to broaden the concept of concentration by capturing the principal-principal shareholder agency relationship.

The firm's capital structure (CS) is crucial to its overall stability; a firm with a strong capital structure can boost its stock returns through an increase in share price. However, over-reliance on debt exposes the firm to financial distress, financial risks, and bankruptcy thereby impacting stock returns. Capital structure is defined as the mixture of common share capital, preferred share capital, term loans, retained profit, debts, and other long-term sources of capital that a business can raise to form part of its total capital (Pandey, 2015). Dieu and Thi (2016) defined capital structure as a mixture of long-standing debt and equity. Debt constitutes that part of the financing that a company receives from its lenders, in the form of loans, bonds, and debentures; while equity concerns that part of the capital funded by the stockholders. Capital structure has been measured using various indicators. Mihai and Mihai (2013) measured capital structure through the debt-to-asset ratio, which measures the long-term liabilities that are attributed to the assets of companies. Higher debt to corporate assets is considered to be riskier to equity investors and vice versa (Madhani, 2016). Berggren and Bergqvist (2015) measured capital structure using the debt-to-equity ratio, which is the proportion of capital contributed by shareholders to each shilling borrowed. In the current study, the capital structure is operationalized through a debt-to-equity ratio as recommended by Berggren and Bergqvist (2015). This ratio is selected because it helps one to know how leveraged the company is, as well as to give stocks that are at high risk to shareholders if the company has a high leverage ratio (Siyanbola et al., 2013).

Stock returns (SR) represent reflection of time compensation, the expected rate of inflation, and the risk of return on investment in stocks (Fama, 1981). Stock returns are important because the movement in stock prices is closely related to changes in macroeconomic variables. This is because the stock markets contain fundamental information about the macro economy and understanding factors that affect stock returns plays a fundamental role in making corporate decisions for better performance. Stock returns are affected by ownership concentration and capital. Ownership concentration has always been presented as an internal governance system that enables greater monitoring and boosts performance (Ongore, 2008). However, because of the potential inefficiency of disciplinary actions brought on by immature capital markets, the impact of ownership concentration on stock performance could be adverse. External block holders may prefer the use of leverage to prevent managers from awarding themselves large perquisites to reduce managerial opportunism. In previous studies, stock returns were measured using return on equity (ROE) and return on asset (Hatem, 2017). ROE was measured as the ratio of the net profit to the share capital. With higher performance, there was an increase in the price of the corporation's stocks, and then a return on the market. The return on assets was measured as the ratio of net profit to total assets, where the increase in shareholder wealth was due to high performance and the return on the stock market. The stock return may also be measured by taking changes in price during the financial year plus any dividends paid, divided by the original price of the stock. This measure is important because it determines the gain from the price change as well as the current dividend paid by the company and therefore gives the total return on the stock.

Stock returns often measured using the Nairobi Securities Exchange 20-Share index have witnessed price and trade volume fluctuations. The 2019/20 fiscal year had a considerable fall in market performance, which could be linked to the market impact of Covid-19. The NSE 20 Share Index, Market Capitalization, and Bonds Turnover all fell by 26.25%, 7.63%, and 4.66%, respectively. Nonetheless, the Equity Turnover and Share Volume jumped by 8.43% and 0.14%, respectively, as a result of the significant panic trading that happened following the disclosure of Covid-19 existence in Kenya (CMA, 2020). Most firms listed at the NSE have mixed ownership structures. Mainly the firms have their ownership composed of individual, institutional, government, foreign and domestic shareholders. The capital markets authority restricts ownership by individuals to not more than 5% of the total shares except where an investor undergoes vetting for ethical values and financial capability by the regulator. The company act 2015 requires branch foreign companies to give 30% of ownership to Kenyan citizens by birth while those incorporated in Kenya can have 100% foreign ownership (CMA, 2016). High levels of ownership concentration are a common feature among listed firms in Kenya with institutional and foreign shareholders accounting for 41% and 34% of total ownership, respectively (Oltetia, 2002). Most listed firms have grown their debt levels over the last decade. According to a report by cyton investments (2019), only 5% of firms listed at NSE sourced their financing from the capital markets while 95% of the firms took bank loans as a source of funding their operations. Maina et al. (2019) reported an increased uptake of bank loans, with most companies keeping away from corporate bonds. According to the cyton (2019) report, the drop in corporate bond issuance was caused by bondholder losses as a result of defaults by various companies including; Nakumatt supermarkets, Imperial Bank, ARM cement, and Chase Bank. In addition, the capital markets authority (2018) report notes that five new listings on the stock exchange occurred between 2013 and 2017, versus a target of four listings annually, indicating that the majority of businesses preferred borrowed funding.

B. Problem Statement

A critical role for management boards, investors, and regulatory bodies is to design and implement regulations, policies, and strategies that enhance stock performance. To achieve this objective, firms require an appropriate level of ownership concentration and capital structure. Ownership concentration is a key corporate control and governance
instrument that addresses the agency problem and enhances firm performance by allowing the majority owners to influence managers’ decisions, align owners' and managers' interests, and escalate owners' monitoring of managers (Crisostomo et al., 2015). Ownership concentration enables majority shareholders to influence the capital structure policies that are independently linked to firm performance. Ideally, firm managers should strive to maximize stock returns by selecting an optimal capital composition that maximizes the trade-off between the cost of leverage and gains. However, with little information being availed to potential investors and the possibility of insider trading, companies with concentrated ownership tend to experience volatility in stock prices (Demsetz & Lehn, 1985).

Researchers linking ownership concentration and stock returns have arrived at different and conflicting results. Panda (2022) found a negative correlation between concentrated ownership and stock returns among Indian firms. Similarly, Clark and Wojcik (2005) contend that performance is negatively affected by ownership concentration after controlling for size due to large capital requirements for big firms, something that cannot be attained unless through expansion of the capital base. On the contrary, Shumali and Abuamsha (2022) found a Positive link between foreign holding, managerial ownership, large ownership and stock returns. The positive effect is confirmed by Zou and Adam (2008) who contend that ownership through large block holders increased stock returns among Chinese firms. Hegde et al. (2020) established that ownership concentration positively affects stock returns. Further, Warrad et al. (2013) indicate that concentrated ownership has no significant effect on stock performance.

Empirical literature linking Ownership concentration, leverage, and stock returns has reported mixed relationships. Berggren and Bergqvist (2015) found that capital structure positively affects stock returns. Rajverma et al. (2018) investigated the relationships among ownership structure and cost of capital in India. Firms with family holdings reported increased leverage and low-cost capital in comparison to non-family-owned enterprises. Mulyani et al. (2016) contend that Ownership concentration through family shareholding affects determination of capital structure among Indonesian firms. Muriungi (2021) examined the influence of ownership concentration on leverage and value of NSE-listed firms. From the results, ownership concentration did not affect firm value while Ownership concentration and leverage had a complimentary impact on the relationship. However, the studies investigated the variables separately and did not consider the mediation effect of capital in the relationship between ownership concentration and stock returns as envisaged in this study.

Ordinary least square (OLS) regression analysis has been applied in past studies to study the link between ownership concentration and stock returns. However OLS does not take care of fixed effects and may lead to misleading results, creating a methodological gap. The current study used panel regression that has greater control of endogeneity due to causal relationships, greater data variability, control of any possible collinearity between variables, and greater information availability (Cheng, 2007). The interrelationship among ownership concentration, capital structure, and stock returns have been examined individually and with mixed and contradictory findings. Further, there is a scarcity of studies on the ownership concentration and stock returns relationship; most studies were conducted in developed countries whose macroeconomic environment is different from the Kenyan context due to different social, political, economic, and regulatory factors. Therefore, the question is: What is the effect of capital structure on the link between ownership concentration and stock returns of companies listed at the Nairobi Securities Exchange?

II. LITERATURE REVIEW

A. Theoretical Review

Agency theory is the anchoring theory of the study because it helps in the conceptualization of how stock returns interact with ownership concentration. The agency theory popularized by Ross and Mitnick (1973) contends that the separation between ownership and management brings forth agency conflicts and seeks the resolution of these problems. Conflict of interest is inevitable in any firm where there is more than one interested party due to a variance of interest between owners and agents (Bosse & Phillips, 2016). The owners are employing managers to increase their wealth but in most cases, managers act contrary to the expectations of their principals and manage the firm to serve their private interests by awarding themselves huge salaries, and allowances and directing the firm's cash to unproductive projects. Agency theory seeks the resolution of agency conflict through the implementation of the best internal governance mechanism to control management actions by recommending two solutions. To begin with, the principals can design performance-based contracts, where the agents' performance can be checked against set targets. Secondly, the principal can gather intelligence information on the actions of his agents; this helps the principal to hold the agents accountable for all their actions by instituting disciplinary actions on errant managers (Jensen & Mechling, 1976).

Agency theory is essential in this research as it represents the interactions between ownership concentration and stock return. It helps understand the relationship between shareholders who are the principals and managers who act as agents. The agency theory informs us of the importance of managing the shareholder-manager relationship to avoid agency conflict, hence enhancing stock returns. The trade-off theory helps in the conceptualization of capital structure in the ownership concentration and stock returns link. The trade-off theory (TOT) was formed by Kraus and Lichtenberger in 1973 who asserted that an ideal capital structure could be achieved when the extra gain from increased debt, equals the extra cost of debt. TOT predicts a positive nexus between Leverage and profitability. Profitability is linked with high stock returns, lower risk of bankruptcy, and consequently lower cost of borrowing. TOT recommends that firms should have an optimal capital structure that helps balance the interest tax shield of debt with the cost of financial distress, agency benefits, and the cost of debt (Culata & Gunarsih, 2012). Optimal leverage will constitute the debt and equity combination that will yield a high value to the firm through high stock prices.
However, market frictions occasioned by refinancing costs may dampen the positive nexus between leverage and profitability. Trade-off theory is significant in this study as it helps the conceptualization of capital structure as a mediator variable in the nexus between ownership concentration and stock returns. The existence of high debt helps to reduce agency problems as managers have to pay debt interest to avoid bankruptcy. Thus, managers have to balance between the interest tax shield benefit of debt and the cost of bankruptcy. TOT envisages that profitable firms will take high debt levels to take the advantage of tax shield benefits as well as increase debt availability which ultimately increases the value of a company (Frank & Goyal, 2008).

B. Conceptual Framework

The conceptual framework (fig1) considers how ownership concentration and capital structure can be employed in decision-making to attain high-quality decisions that would improve stock returns as a dependent performance variable in firms. Stock return is the dependent variable because it can be influenced by management decisions, and will be measured through capital gain or loss plus any dividend paid on the shares divided by the original value of the share. This measure is important because it factors in the capital gain from the change in the price of the stock as well as the current earnings from the dividend paid by the firm and hence giving out the total return from the stock. Ownership concentration is the independent variable operationalized through the percentage of shares possessed by the five largest shareholders. It has been demonstrated empirically that ownership concentration can be used as a governing mechanism to address the principal-agent agency problem thus resulting in greater competitiveness and performance of concentrated firms. Ownership concentration increases the value of a company by incentivizing the majority shareholders to engage in monitoring behaviours that reduce agency costs of sub-optimal managers’ decisions, cost structuring, and agent behaviours that conflict with shareholders. Capital structure operationalized through debt to equity ratio is assumed to intervene in the relationship between ownership concentration and stock returns. The level of ownership concentration affects the capital structure adopted by the firm due to the influence of the majority shareholder(s) based on their appetite for risk.

Capital structure significantly affects performance, the value of the firm, and the cost of capital. Debt to equity ratio is important because it assists one to know how levered a company is as well as gives stocks that are of high risk to shareholders if the firm has a high leverage ratio.

H0: Capital structure has no intervening role in the relationship between ownership concentration and stock returns of firms listed at the Nairobi Securities Exchange.

III. METHODOLOGY

A. Data

The research used secondary panel data on Ownership concentration, capital structure and stock returns from 2006 to 2019. This period was selected because in 2006 the NSE introduced the Automated Trading System (ATS) which lead to the automatic matching of orders and execution of the same by stockbrokers. The efficiency of order initiation and execution leads to a more accurate market value of the stocks which is approximate to the intrinsic value of the stock. Data relating to ownership concentration was obtained from audited books of accounts published on the firm’s websites, NSE database and licensed data vendors after payment of requisite fees. Consequently, data on the number of stocks held by the five largest shareholders and the total number of stocks outstanding was collected.

The study also collected data on the capital structure which included the total book value of debt and the market value of shareholders’ equity (closing MPS*outstanding shares). Data on the MPS was obtained from the NSE database and NSE licensed data vendors after payment of requisite fees. To calculate the stock returns, we collected data on the opening Market price per share, closing MPS and Dividend per share. Data on opening MPS and closing market price per share was collected from NSE and NSE licensed data vendor’s websites while data on DPS was sourced from audited books of accounts published in the company’s websites, NSE database and licensed data vendors after payment of requisite fees.

B. Data Analysis

Before doing inferential analysis, descriptive analysis was performed to illustrate the distribution of data, spot outliers, and identify correlations between the variables. The correlation coefficient (r) was used to measure the strength of the association and was stated at 0.05 significance. Diagnostic tests of multicollinearity, normality, stationarity, serial correlation and heteroskedasticity were undertaken before data analysis to check on the assumptions of the model. Panel regression analysis was utilized to conduct test of hypothesis. To determine the intervening effect of capital structure, the Baron and Kenny (1986) four-step model was used. For mediation to exist in step one, ownership concentration must relate directly to stock returns. In step two, the ownership concentration must relate directly to capital structure. In step three there must be a statistically significant relationship between the capital structure and stock returns. Finally, in step four, Baron and Kenny (1986) suggest that the beta coefficient of ownership concentration becomes insignificant for a full mediation to have occurred. In the first step, stock returns were regressed against ownership concentration.
The panel regression model was as stated in (1).

$$SR_{it} = \beta_0 + \beta_1 OC_{it} + \varepsilon_{it}$$  (1)

The independent variable must relate directly to the mediating variable in step two. Baron and Kenny (1986) suggest that there must be a significant relationship between the predictor and the intervening variables in the absence of the response variable. In the second step, Capital Structure was regressed on ownership concentration, as shown in (2), and the significance of the coefficient of capital structure was noted.

$$CS_{it} = \beta_0 + \beta_2 OC_{it} + \varepsilon_{it}$$  (2)

For the intervention to exist in step three, Baron and Kenny (1986) suggest that there must be a significant relationship between the intervening variable and the dependent variable. In the third step, the stock returns were regressed on capital structure, as shown in (3), and the significance of the coefficient of stock return was noted.

$$SR_{it} = \beta_0 + \beta_3 CS_{it} + \varepsilon_{it}$$  (3)

For full mediation to occur in step four, the direct relationship between ownership concentration and the stock returns becomes insignificant (Baron and Kenny, 1986). Alternatively, the effect reduces materially for a partial intervention to have occurred. In the fourth step, stock returns were regressed on both ownership concentration and capital structure, as shown in (4), and the significance of the coefficient of ownership concentration and capital structure was noted.

$$SR_{it} = \beta_0 + \beta_4 OC_{it} + \beta_5 CS_{it} + \varepsilon_{it}$$  (4)

where,

- $SR_i=$Stock Returns,
- $OC_i=$Ownership concentration,
- $CS_i=$Capital Structure,
- $\beta_0=$intercept, which is independent of i and t,
- $\beta_1$ to $\beta_5=$coefficients of variables,
- $\varepsilon_{it}=$ the error term.

IV. FINDINGS AND DISCUSSION

To provide an overall trend about the data for all the variables; the mean, standard deviation, minimum and maximum observations are all included in Table I.

<table>
<thead>
<tr>
<th>Table I: Panel Variables Summary Statistics</th>
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<tr>
<td>Variable</td>
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<tr>
<td>Stock return</td>
</tr>
<tr>
<td>Ownership concentration</td>
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<tr>
<td>Capital structure</td>
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Unbalance panel data of 60 firms listed at NSE from 2006 to 2019

Table I above shows that the total units of observation were 719, unlike the estimated 840 observations. This is because the study used unbalanced panel data and the fact that the data category was not observed in some years. From the output in Table I, the outcomes indicate that the mean stock return over the period was 0.243. These results suggest that on average stock returns as measured by the change in price plus cash distribution as a percentage of the initial cost was 24.3%. The accompanying standard deviation of 0.44 indicates rather significant stock return variability, indicating that individual company stock returns typically deviate from the mean by up to 44%. The results match the lowest and highest values, which are 4.86 and 2.55, respectively. It is established that while some listed firms posted negative returns associated with a decline in share price and diluted dividends, others reported high returns of 255%. The outcomes also show that firms listed on the NSE had a mean ownership concentration of 66% over the analysis period. These results suggest that on average ownership concentration was 66%, indicating that for a majority of listed firms, the largest proportion of shares is owned by the top five largest shareholders. The corresponding standard deviations of 16.9% suggest there is a relatively low variability of ownership concentration among the listed firms. However, the spread is wide, with a minimum of 11% and a maximum of 97%. This means that while some listed firms had low ownership concentration, others had very high concentration. Regarding, capital structure, the research established that the average debt-to-equity ratio was 0.672 indicating that the majority of the listed firms had borrowed 0.672 shillings for every shilling contributed by ordinary shareholders. The standard deviations of 1.81 suggest that there were high variations in the debt-to-equity ratio among the listed firms. This meant that on average the debt-to-equity ratio of individual firms varied from the mean by 1.81. The high value suggests that there were high variations such that while some firms had a debt-to-equity ratio of as low as zero (0) others had a high debt-to-equity ratio of 4.663. A minimum debt-to-equity ratio of zero (0) suggests that some listed firms were all equity financed and had no debt in their leverage. However, a debt-to-equity ratio of 4.663 indicates that for every shilling contributed by the shareholders, the company has borrowed sh. 4.663. This indicates high levels of leverage which may expose the company to financial risk, financial distress, and ultimately liquidation. The link between stock returns and ownership concentration was weak and negatively correlated. Diagnostic test for normality revealed that the data was not normally distributed. To address the lack of normality, the data were transformed using natural logarithms. The use of logarithmic transformation tends to provide values that approximate a normal distribution and for which conventional linear regressions and analysis of variance models are appropriate (Petrie et al., 2002). The panel regression model showed a statistically significant and negative linear relationship between stock returns and ownership concentration ($\beta_1 = -0.107$, P-value = 0.026). Meaning for every 1% increase in ownership concentration, stock return decreased by 10.7%. The overall model was significant ($\beta = 1.601$, overall- $R$ squared = 0.083, P-value = 0.000, $F = 4.957$). The adjusted $r^2$ of 0.083 implied that 8.3% of the variations in stock returns were explained by ownership concentration. The findings are in line with Baron and Kenny (1986) that the predictor must affect the response variable for mediation to exist, hence the study progressed to step two of assessing mediation. A summary of step one findings is shown in Table II.

The results of step two shown in Table III above indicate a statistically significant and positive link between ownership concentration and the mediator, capital structure (β = 0.209, P-value = 0.001). These results imply that a 1% change in ownership concentration leads to an increase in capital structure by 20.9%. The overall model is significant (Adjusted R-squared = 0.0665, F-statistic = 15.039, P<0.05) and explains 6.65% of the variations in capital structure explained by ownership concentration. The findings are in line with Baron and Kenny (1986) that the predictor must affect the mediator variable for mediation to exist, hence the study progressed to step three of assessing mediation.

In step three, the mediator must have a direct and significant nexus with the response variable. The findings in Table IV above indicate a statistically significant and positive nexus between stock returns and capital structure (β = 0.17, P-value = 0.001). These results imply that a 1% change in capital structure leads to a decrease in stock returns by 17%. The overall model is statistically significant since the P-value is < 0.05 (Adjusted R-squared = 0.0718, F-statistic = 11.849, P<0.05). The Adjusted r-squared implies that capital structure accounted for 7.18% of the variations in stock returns. In step four, the effect of the ownership concentration on the stock returns becomes statistically insignificant for full mediation to occur when the study accounts for the mediation effect in the model. Table V shown above indicates an insignificant negative relationship between Stock returns and ownership concentration (β = -0.063, P-value = 0.631). The results also revealed a significant and negative nexus between stock returns and capital structure (β = -0.17, P-value = 0.001). The overall model produced an Adjusted r-squared of 0.0731, F=6.033, and P<0.05. This meant that ownership concentration and capital structure jointly explain 7.31% of the variation in stock returns. From the results in step 4, the beta coefficient of ownership concentration became statistically insignificant after controlling for capital structure (β = -0.063, P-value = 0.631). Thus, Based on Baron and Kenny (1986) approach, these results suggest that capital structure mediates the relationship between ownership concentration and SR. Hence, the null Hypothesis (H0) was rejected.

The finding of a positive relationship between ownership concentration and capital structure is consistent with Mustafa and Wasfi (2016), Ceylan (2018) and Okiro et al. (2015). The results of a direct negative association between capital
structure and stock returns conflict with Berggren and Bergqvist (2015) who observed that leverage had a positive effect on stock returns, Sari and Patrisia (2019) who reported that capital structure positively impacts firm value in Real estate firms and Zhang (2006) who observed that change in leverage has no effect on stock returns. The findings of a negative relationship between capital structure and stock returns imply that firms need to maintain their leverage up to a certain level to avoid the adverse effects of too much leverage and ensure the firm maximizes the tax shield benefit of debt to maximize returns. Kraus and Litzenberger (1973) contend that an ideal capital structure could be achieved when the extra gain from increased debt, equals the extra cost of debt. The conflicting findings could be because empirical studies examined the relationship between ownership concentration, capital structure and stock returns separately. The current study examined the intervening effect of capital structure on the link between ownership concentration and stock returns and confirmed the effect.

V. CONCLUSION, LIMITATIONS AND RECOMMENDATIONS

A. Conclusion

This study examined the mediating effect of capital structure on the ownership concentration and stock returns relationship. The hypothesis test results found that capital structure mediates the Nexus between ownership concentration and stock returns. This implies that capital structure has the potential effect of adversely affecting stock returns as shareholders keep away from firms with high levels of debt in their capital structure by selling their shares leading to a drop in the share price which negatively impacts stock returns. A possible explanation is that Kenya’s financial sector is still emerging and may not adequately screen the use of funds advanced to firms to reduce agency costs. The lack of enough regulations in the Kenya market implies that managers may advance their interest by diverting borrowed funds to unproductive investments thus negatively impacting firm performance and adversely affecting stock returns. Therefore, Capital structure is critical in explaining the relationship between ownership concentration and stock returns. This connection should be encouraged through appropriate policies that ensure capital is channeled towards productive projects that seek to maximize the wealth of shareholders. The interest of all stakeholders must be protected to avoid majority shareholders exploiting them through ownership concentration. Debt holders should enter into contracts to have representatives on the board to ensure their debt covenants are adhered to. Governments should take some ownership stake to ensure companies comply with laid down policies and procedures and promote a transparent social, political and economic environment for listed firms. This will promote and enhance corporate performance and increase stock returns.

B. Limitations

Although there were minimal limitations in this study, caution was taken to ensure that they did not negatively impact the findings. First, the study assumed that ownership concentration, Capital Structured, and stock returns are all linearly related. However, the current study did not take into account the possibility of other types of relationships, such as curve linear relationships, particularly concerning the nexus between ownership concentration and stock returns. To cater for this limitation the study used panel regression with fixed effects.

C. Suggestion for Future Research

To determine whether the findings would hold in various circumstances, a comparable study may be conducted in other emerging and developed nations. Given the differences in social, political, regulatory, and economic dynamics between nations, it would be interesting to identify the type of interaction. In the future, performance metrics other than stock returns, like Return on equity, Return on assets, and Tobin’s Q, can be used to examine whether there is a connection between ownership concentration and leverage.

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