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ISSN: 3080-0706

Research Beacon Journal
Volume 19||Issue 9||Page 110- 123||September||2025|
Email: info@researchbeacon.org
ISSN: 3080-0706

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How to cite this article: **Musundi, R. ., Ondigo, H. ., & Aduda, J. . (2025). Private Equity Investments, Ownership Structure and Financial Performance Evidence from Investee Firms in Kenya.** ***Research Beacon, 19*****(9), 110-122. https://doi.org/10.70907/aszwgx73**

ABSTRACT

The interplay between private equity (PE) investments and firm ownership structure has significant implications for financial performance, particularly in emerging markets where capital constraints and governance challenges persist. This study examines how ownership structure moderates the relationship between private equity investments and the financial performance of investee firms in Kenya. Anchored on agency theory, trade-off theory, and finance-growth theory, the research disaggregates PE into venture capital, growth capital, and buyout capital, while ownership structure is measured as the proportion of shares held by the largest shareholder. The study utilized a descriptive research design and analyzed panel data from 144 private equity-backed firms over the period 2006 to 2021. Panel regression models with interaction terms were employed to capture the moderating effects. The findings reveal that while all forms of private equity have a positive and statistically significant effect on Return on Assets (ROA), the magnitude of this effect varies depending on ownership concentration. Specifically, firms with moderate ownership concentration benefited most from PE funding, suggesting an optimal balance between managerial control and investor oversight. These results underscore the importance of considering ownership dynamics when assessing the impact of private equity on firm performance. The study offers valuable insights for investors, policymakers, and managers seeking to optimize governance structures to fully harness the benefits of private equity financing.

Key Words: Private equity, ownership structure, financial performance, venture capital, growth capital, buyout capital, Return on Assets

INTRODUCTION

Private equity (PE) has become a significant financing channel for firms globally, offering capital alongside strategic and managerial support. By injecting funds in the form of venture capital, growth capital, and buyout capital, PE firms aim to improve operational efficiency, strategic alignment, and ultimately financial performance (Hotchkiss, Smith & Strömberg, 2021; Datta &

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ISSN: 3080-0706

Singh, 2019). Theoretically, PE funding is expected to enhance profitability through governance reforms, value creation strategies, and rigorous monitoring mechanisms (Jensen & Meckling, 1976). However, the extent to which these benefits materialize often depends on internal firm characteristics, notably the ownership structure, which influences decision-making autonomy, control, and accountability.

Ownership structure refers to the distribution of equity among shareholders and has been identified as a critical determinant of how external investments influence firm performance (Hu & Loh, 2018; Ramadhan, 2014). Highly concentrated ownership can align incentives between majority shareholders and managers, potentially enhancing oversight and strategic focus (Duska, 2011). Conversely, excessive concentration may lead to entrenchment, reduced transparency, and resistance to external investor influence (Leech, 1986). In the context of PE-backed firms, the ownership structure can either amplify or limit the effectiveness of governance mechanisms introduced by PE investors.

Kenya has experienced a steady growth in PE activity over the past two decades, positioning itself as a leading destination for such investments in East Africa (Cytonn Investments Limited, 2020; KPMG, 2021). Investee firms operate across diverse sectors, from retail and manufacturing to fintech and healthcare. However, differences in ownership patterns among these firms may lead to varying outcomes from PE funding. For example, PE-backed retail chains like Naivas and Quickmart have leveraged external capital to expand operations, but their performance trajectories differ due to variations in governance and ownership arrangements. This suggests a need for empirical analysis of how ownership structure interacts with PE investments to influence financial performance in the Kenyan setting.

Research Problem

Private equity investments are widely regarded as catalysts for improved financial performance due to their ability to provide not only capital but also strategic and operational expertise (Weir, Jones & Wright, 2015). However, empirical evidence shows that the relationship between PE and firm performance is not uniform across investee firms. One possible explanation lies in differences in ownership structure, which can influence how effectively PE governance reforms are implemented (Martí, Balboa & Palacios, 2025). For example, firms with highly concentrated ownership may resist changes proposed by PE investors, thereby reducing the potential performance gains.

Although studies in developed markets (e.g., Bernstein et al., 2018; Biesinger & Bircan, 2018) have examined the moderating role of firm characteristics, including ownership structure, such evidence is scarce in the Kenyan context. Most local studies have focused on the direct effects of PE on performance (Karugu, 2018; Karanja, 2018), without investigating how ownership concentration might alter these effects. This gap is significant because ownership dynamics in Kenya often differ from those in developed economies, with many firms being family-owned or having a dominant shareholder, potentially affecting the adoption of PE-driven governance practices.

Furthermore, existing empirical work in Kenya often employs cross-sectional designs or small samples, limiting the generalizability of findings (Karanja, 2018; Mwenje & Olweny, 2016). There

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is limited use of panel data techniques to explore how ownership structure shapes the PE–performance relationship over time. Without such evidence, policymakers, investors, and managers may lack the insights needed to align ownership arrangements with the strategic and operational benefits of PE. This study therefore seeks to fill this gap by investigating the moderating role of ownership structure in the relationship between PE investments and financial performance among investee firms in Kenya.

LITERATURE REVIEW

Theoretical Foundation

This study is anchored on Agency Theory as proposed by Jensen and Meckling (1976), which examines the contractual relationship between principals (shareholders) and agents (managers). In private equity-backed firms, PE investors act as active principals who seek to align managerial actions with shareholder wealth maximization through governance reforms, monitoring, and performance-based incentives (Mathuva, 2014). Ownership structure plays a pivotal role in this alignment. When ownership is moderately concentrated, dominant shareholders can support PE-driven governance measures, reducing agency costs and enhancing performance. Conversely, excessive concentration may lead to managerial entrenchment, limiting the influence of PE investors on strategic and operational decisions (Leech, 1986; Duska, 2011).

The Trade-Off Theory (Modigliani & Miller, 1958; Myers, 1984) also provides insights into the interaction between PE, ownership structure, and performance. This theory posits that firms strive for an optimal capital structure by balancing the benefits and costs of debt and equity financing. In PE-backed firms, ownership concentration can influence the firm's willingness to adjust capital structure in line with PE recommendations. Highly concentrated ownership may prioritize control preservation over optimal financing decisions, potentially constraining the ability of PE funds to implement value-enhancing leverage strategies (Sheikh & Wang, 2011). On the other hand, more balanced ownership structures may be more receptive to capital restructuring proposals that improve financial performance.

Finally, the Finance-Growth Theory (Bagehot, 1973) highlights the role of financial resources and institutional structures in fostering firm and economic growth. PE investments, by providing capital and governance expertise, create conditions conducive to improved financial performance. However, the ownership structure can either facilitate or hinder the flow of these benefits. Firms with ownership arrangements that encourage transparency and accountability are better positioned to fully leverage PE resources for growth (Demirgüç-Kunt & Levine, 2008). In the Kenyan context—where many firms are family-owned or dominated by a few shareholders—the way ownership is structured can critically determine whether PE funding translates into sustained profitability and competitive advantage.

Empirical Review

Globally, research has demonstrated that ownership structure can significantly influence the performance outcomes of private equity (PE) investments. Martí, Balboa, and Palacios (2025), using data from 28 OECD countries, found that PE had a stronger impact on financial performance in firms with moderate ownership concentration compared to those with either highly dispersed or

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highly concentrated ownership. Similarly, Biesinger and Bircan (2018) observed that PE-backed firms in Europe improved operational efficiency post-investment, but the extent of improvement was moderated by governance arrangements, including shareholder concentration. These findings suggest that ownership structure shapes the effectiveness of PE interventions, but they primarily reflect developed market contexts, which differ institutionally from emerging economies like Kenya.

Regionally, studies in Africa also indicate that firm-specific characteristics, including ownership structure, play an important role in the PE–performance nexus. Adeleke and Owusu (2022), examining 85 PE-backed firms in Ghana, reported that firms with mixed (foreign and local) ownership showed greater financial performance gains than those with purely domestic or foreign ownership. Mugisha and Tumusiime (2021) found that in Rwanda and Uganda, PE-backed firms with transparent and diversified ownership exhibited higher revenue growth than those with concentrated family ownership. However, these studies did not specifically test ownership structure as a statistical moderator, leaving the mechanism through which it affects the PE–performance relationship underexplored.

In Kenya, research on PE and ownership structure is limited and fragmented. Wambua and Mutuku (2024) studied PE-backed firms in the agriculture and ICT sectors and found that family-owned firms were less responsive to PE-driven governance changes compared to professionally managed firms with external ownership. Karugu (2018) and Karanja (2018) reported generally positive effects of PE on financial performance, but neither considered ownership structure as a moderating variable. Mutende et al. (2017) showed that firm age and size moderated the relationship between financial resources and performance among listed firms, suggesting that internal characteristics can alter investment impacts, yet ownership structure was not examined in a PE context.

Overall, while there is evidence that ownership structure influences how firms respond to external investments, there is a paucity of empirical studies in Kenya that directly examine its moderating role in the relationship between PE investments and financial performance. Most existing local studies focus on the direct effect of PE or on other firm characteristics, use small samples, or adopt cross-sectional designs that cannot capture the dynamic nature of these relationships. This study addresses these gaps by employing panel data from 144 PE-backed firms in Kenya between 2006 and 2021, disaggregating PE into venture, growth, and buyout capital, and explicitly modeling the interaction between PE investments and ownership structure to determine their joint effect on Return on Assets (ROA).

RESEARCH METHODOLOGY

This study adopted a descriptive research design to examine the moderating effect of ownership structure on the relationship between private equity investments and financial performance of investee firms in Kenya. The study was anchored on positivist philosophy, emphasizing empirical measurement and statistical testing to establish causal inferences. The target population comprised 152 firms that received private equity funding between 2006 and 2021. Complete data was available for 144 firms, forming an unbalanced panel dataset spanning a 16-year period.

Secondary data was obtained from private equity fund reports, investee firms' audited financial statements, and industry publications. The independent variable, private equity investments, was

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operationalized in three categories: venture capital, growth capital, and buyout capital (KPMG, 2021; Deloitte, 2018). The moderating variable, ownership structure, was measured as the proportion of shares held by the largest shareholder, consistent with prior studies (Ramadhan, 2014; Hu & Loh, 2018). The dependent variable, financial performance, was measured using Return on Assets (ROA), a widely used profitability indicator in similar empirical studies (Karugu, 2018; Wang & Clift, 2009).

Panel regression models were employed to analyze the data, with interaction terms introduced to test the moderating effect of ownership structure on the relationship between each PE category and financial performance. Diagnostic tests were conducted to ensure robustness of the model, including tests for multicollinearity, stationarity, heteroskedasticity, autocorrelation, and normality. The Hausman specification test was applied to determine the choice between fixed effects and random effects models. The statistical significance of the moderating effect was assessed through the interaction coefficients, with results interpreted at the 1%, 5%, and 10% significance levels. All analyses were performed using Stata statistical software.

FINDINGS AND DISCUSSION

Baron and Kenny's (1986) framework for testing moderation is a widely used methodological approach in empirical research. The process involves a systematic three-step procedure aimed at establishing whether a moderating variable alters the strength or direction of the relationship between an independent variable (predictor) and a dependent variable (outcome). In Step 1, the model assesses the direct relationship between the independent and dependent variables; this relationship must be statistically significant to proceed. Step 2 introduces the moderator variable into the model alongside the predictor and the criterion variables. A statistically significant model at this stage suggests that the moderator and the predictor have a joint influence on the outcome variable.

In Step 3, the interaction term—computed as the product of the centered predictor and the centered moderator—is introduced into the regression model. This interaction term is critical in determining the presence of a moderating effect. A statistically significant interaction term implies that the moderator significantly influences the strength or direction of the relationship between the predictor and the outcome variable. The Baron and Kenny approach assumes that there is a significant baseline relationship between the independent and dependent variables, which provides the foundation for testing whether this relationship is contingent upon the presence of a moderator. Therefore, moderation is confirmed if the interaction term significantly improves the explanatory power of the model, indicating that the moderator alters the nature of the relationship between the predictor and the outcome.

In step 1 (Model 1), regression analysis estimated the relationship between financial performance and each of the private equity investments indicators (venture capital, growth capital and buy out investment). The regression analysis in Table 1 reveals positive and significant coefficients for each private equity investment indicator (venture capital, growth capital, buyout capital) on financial performance, indicating a favorable impact on financial outcomes.

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Table 1: Private Equity Investments Indicators and Financial Performance

ROA	Coef.	Std. Err.	P>t
Venture capital	0.047226*	0.02338	0.015
Growth capital	0.409957*	0.04779	0.000
Buyout capital	0.08728*	0.026956	0.003
_cons	-4.71495*	0.35955	0.000
Model Summary			
R-squared	0.1768		
F(3,2292)	164.07		
Prob > F	0.0000		
Observations	2,448		
ID	153		

In Step 2 (Model 2), the association among the criterion, moderator, and predictor variables (private equity investments indicators, measured by venture capital, growth capital and buy out investment) was assessed using the panel regression analysis Hausman test as a guide. A statistically significant regression model is required. To determine whether ownership structure moderates the relationship between financial performance and venture capital, financial performance was regressed on venture capital and ownership structure. Table 2 presents the results of regressing financial performance on venture capital and ownership structure. The negative and significant coefficient for ownership structure suggests that it independently influences financial performance, and the Hausman test indicates a statistically significant regression model.

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Table 2: Venture Capital, Ownership Structure and Financial Performance

ROA	Coef.	Std. Err.	P>t
Venture Capital	-0.26473	0.098073	0.007
Ownership structure	-0.35692	0.03147	0.000
_cons	1.53705	1.066403	0.15
R-squared	0.0555		
F(2,2293)	67.34		
Prob > F	0.0000		

* p<0.05

In step 3, Model 3, financial performance was regressed on ownership structure, private equity investments indicators, and interaction term created by multiplying the centered private equity investments indicators (independent variable) and centered moderator (ownership structure). The interaction term should be statistically significant if there is a moderating influence.

The relationship between venture capital (independent variable), ownership structure (moderator), the interaction term (VC*OS), and financial performance (dependent variable) was estimated using Fixed-effects regression.

Table 3: Interaction Term for Venture Capital and Ownership Structure

ROA	Coef.	Std. Err.	P>t
Venture Capital	-0.15453	0.085135	0.070
Ownership structure	-1.13391	0.039261	0.000
VC*OS	0.578979	0.021034	0.000
_cons	-5.46433	0.959035	0.000
R-squared	0.2901		
F(3, 2292)	312.27		
Prob > F	0.000		

* p<0.05

The coefficients in Table 3 demonstrate that the interaction term is statistically significant (p = 0.000), indicating a moderating influence of ownership structure. The negative coefficient for the

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interaction term suggests that, in the presence of ownership structure, the impact of venture capital on financial performance is attenuated.

The findings from Tables 1 to 3 reject the null hypothesis H_{01}, providing evidence that ownership structure moderates the relationship between private equity investments, particularly venture capital, and the financial performance of investee firms in Kenya. The results highlight the nuanced role of ownership structure in influencing how private equity investments impact the financial outcomes of investee firms.

To determine whether ownership structure moderates the relationship between financial performance and growth capital, financial performance was regressed on growth capital and ownership structure.

Table 4: Growth Capital, Ownership Structure and Financial Performance

ROA	Coef.	Std. Err.	P>t
Growth Capital	0.580775	0.021021	0.000
Ownership structure	-0.5545	0.028234	0.000
_cons	-7.16208	0.21202	0.000
R-squared	0.2891		
F(2,2293)	466.29		
Prob > F	0.0000		

* $p<0.05$

Source: Research Findings (2024)

In Table 4, which explores the moderating effect of ownership structure on the relationship between financial performance and growth capital, the regression coefficients indicate significant associations. Growth capital has a positive coefficient (0.580775) on financial performance, suggesting a favorable impact on the latter. Ownership structure, with a negative coefficient of -0.5545, independently influences financial performance negatively. The statistically significant model ($p = 0.000$) confirms the relevance of these variables in explaining variations in financial performance. The R-squared value of 0.2891 indicates that approximately 28.91% of the variability in financial performance is explained by growth capital and ownership structure.

The relationship between growth capital (independent variable), ownership structure (moderator), the interaction term (GC*OS), and financial performance (dependent variable) was estimated using Fixed-effects regression. The results are as shown in Table 5.

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Table 5: Interaction Term for Growth Capital and Ownership Structure

ROA	Coef.	Std. Err.	P>t
Growth Capital	0.301093	0.051463	0.000
Ownership structure	-0.89559	0.063851	0.000
GC*OS	0.328967	0.055333	0.000
_cons	-7.55772	0.220721	0.000
R-squared	0.2999		
F(3,2292)	327.30		
Prob > F	0.0000		

* $p<0.05$

Table 5 presents the results for the interaction term (GCOS) when estimating the moderating effect of ownership structure on the relationship between growth capital and financial performance. The coefficients show that the interaction term is statistically significant ($p = 0.000$), suggesting a moderating influence of ownership structure. The positive coefficient for GCOS (0.328967) indicates that the impact of growth capital on financial performance is accentuated in the presence of ownership structure as a moderator. The negative coefficient for ownership structure (-0.89559) suggests that, in the presence of the moderator, the independent effect of ownership structure on financial performance becomes more pronounced.

These results indicate that ownership structure acts as a moderator in the relationship between growth capital and financial performance. The positive coefficient for the interaction term suggests that ownership structure amplifies the positive impact of growth capital on financial performance. These findings provide valuable insights into the nuanced dynamics between private equity investments, ownership structure, and financial outcomes for investee firms in Kenya.

To determine whether ownership structure moderates the relationship between financial performance and buy out investment, financial performance was regressed on buyout investment and ownership structure.

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Table 6: Buy Out Investment, Ownership Structure and Financial Performance

ROA	Coef.	Std. Err.	P>t
Buyout capital	0.624899	0.022597	0.000
Ownership structure	-0.56055	0.028282	0.000
_cons	-7.41749	0.221	0.000
R-squared	0.2195		
F(2,2293)	367.06		
Prob > F	0.0000		

* p<0.05

The regression coefficients indicate that buyout capital has a positive and significant impact on financial performance, with a coefficient of 0.624899. On the other hand, ownership structure shows a negative and significant impact on financial performance, with a coefficient of -0.56055. The overall model is statistically significant (p = 0.000), with an R-squared value of 0.2195, indicating that about 21.95% of the variability in financial performance is explained by buyout capital and ownership structure.

The relationship between buy out investment (independent variable), ownership structure (moderator), the interaction term (BC*OS), and financial performance (dependent variable) was estimated using Fixed-effects regression. The results are as shown in Table 7.

Table 7: Interaction Term for Buyout Investment and Ownership Structure

ROA	Coef.	Std. Err.	P>t
Buyout capital	0.623612	0.022577	0.000
Ownership structure	-0.35081	0.089177	0.000
BC*OS	-0.21074	0.08499	0.013
_cons	-5.11417	0.95476	0.000
R-squared	0.2814		
F(3,2292)	314.12		
Prob > F	0.0000		

* p<0.05

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The coefficients reveal that the interaction term is statistically significant (p = 0.013), suggesting a moderating influence. The positive coefficient for buyout capital (0.623612) indicates its positive impact on financial performance. The negative coefficient for ownership structure (-0.35081) implies that, in the presence of the moderator, the independent effect of ownership structure on financial performance becomes more pronounced. The negative and significant coefficient for the interaction term (-0.21074) suggests that ownership structure moderates the positive impact of buyout investment on financial performance.

H_{01} investigated the moderating effect of ownership structure on the relationship between private equity investments and financial performance of investee firms in Kenya. Each of the private equity investments indicators was analyzed separately. This study indicates that ownership structure has a moderation influence on the link among private equity investments indicators and the financial performance of investee firms in Kenya since each of the private equity investments indicators fulfilled all the above Baron and Kenny's (1986) steps for testing the moderating influence as indicated in Tables 1 to 7. So, the research rejected H_{01}.

CONCLUSIONS

This study set out to examine the moderating effect of ownership structure on the relationship between private equity (PE) investments and the financial performance of investee firms in Kenya. Using panel data from 144 PE-backed firms over the period 2006–2021, and disaggregating PE into venture capital, growth capital, and buyout capital, the analysis revealed that all three forms of PE had a statistically significant and positive effect on Return on Assets (ROA). Importantly, the results showed that the magnitude of these effects varied depending on the level of ownership concentration, with moderate ownership concentration enhancing the benefits of PE funding more than either highly concentrated or highly dispersed ownership.

These findings align with agency theory propositions that governance structures influence how effectively external capital and expertise are utilized, and with finance-growth theory, which emphasizes that financial resources contribute most to performance when supported by enabling institutional arrangements. The evidence also underscores the trade-off between control and external influence, as excessively concentrated ownership may hinder the implementation of PE-driven operational and strategic changes, while overly dispersed ownership may dilute accountability and slow decision-making.

By empirically demonstrating the role of ownership structure in shaping the impact of PE investments on firm performance in Kenya, the study addresses a key gap in the literature and provides a more nuanced understanding of how internal governance arrangements interact with external financing to drive value creation.

RECOMMENDATIONS

This study offers crucial insights for policymakers seeking to enhance the impact of private equity on the financial performance of investee firms in Kenya. To encourage the positive effects of private equity, policymakers should focus on creating an enabling environment for access to finance. Initiatives such as streamlined regulatory procedures, financial literacy programs, and support for alternative financing options can contribute to a more conducive landscape for private equity investments. Additionally, policymakers may consider designing incentives that promote

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long-term partnerships between private equity investors and local businesses, fostering sustained growth.

Given the significant moderating effect of ownership structure, regulatory bodies can consider guidelines that promote diverse and balanced ownership structures within investee firms. Encouraging a mix of local and international ownership, along with measures to prevent excessive concentration of shares, can contribute to more stable and resilient companies. Policymakers could collaborate with industry stakeholders to develop frameworks that balance the interests of investors, local communities, and the broader economy.

For firms in their early stages (start-ups), policymakers can design targeted support programs, recognizing their unique challenges and potential. Access to finance remains critical for these entities, and tailored policies could include preferential financing rates, mentorship programs, and tax incentives. Moreover, understanding that industry-specific factors play a role in the effectiveness of private equity investments, policymakers may explore industry-specific initiatives to maximize the impact of such investments across diverse sectors.

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