

**Directors' Remuneration and Firm  
Performance in a study of Nairobi Stock  
Exchange Listed Companies**

**Submitted by Geoffrey Ikavulu Injeni  
Reg. Number: 008654 to Strathmore University**

**A thesis submitted in partial fulfilment of the Master of  
Commerce**

**Faculty of Commerce**

**Date: December, 2010**

This thesis is available for library use on the understanding that it is copyright material. No quotation from this thesis may be published without proper acknowledgement.

## DECLARATION

I declare that this work has not been previously submitted and approved for the award of a degree by this or any other University. To the best of my knowledge and belief, this thesis contains no material previously published or written by another person except where due reference is made in the thesis itself.

Signed.....

Date.....

This thesis has been submitted for examination with my approval as the University Supervisor.

Signed.....

Dr. X. N. IRAKI

Date.....

## **ABSTRACT**

Under the agency theory, directors who act as agents of shareholders may benefit from the company by awarding themselves high remuneration. To resolve this problem, some authors have recommended corporate governance principles which include a requirement to pay directors based on firm performance. Examples of pay based on firm performance include bonuses and stock options. In Kenya, companies listed on the Nairobi Stock Exchange (NSE) are required to comply with the corporate governance principles issued by the Capital Markets Authority (CMA), which require directors' remuneration to be based on firm performance. The purpose of the study was to find out first, whether there is a relationship between directors' remuneration and firm performance for Nairobi Stock Exchange companies, and secondly, the components of executive pay together with the key factors that determine executive pay. A regression analysis involving 37 NSE listed companies covering the period between 2003 and 2008 showed the majority of the companies reported a weak positive relationship between executive remuneration and firm performance (when measured by Revenue Growth, Net Profit Margin, Return on Investment, Return on Equity and Earnings per Share), and a weak negative relationship between executive remuneration and stock market returns (measured by Share Price Growth). In addition, an analysis of 23 respondents from the 37 companies also found salaries, fees and other benefits to be the key components of executive pay. Majority (60%) of the respondents mainly consider experience and qualifications to be the key factors that determine executive pay. The study has confirmed the inconsistency of pay based performance in Kenya. The study has also highlighted the key determinants of directors' remuneration for companies listed on the NSE. Further studies can be done to establish the challenges of implementing performance based pay in NSE companies. In addition, further research can be done on performance based pay for small and medium sized firms and in the public and private sectors.

**Key Words:** Directors' remuneration, Firm performance, Agency theory, Corporate governance and Nairobi Stock Exchange

## CONTENTS

|                                                       | Page No. |
|-------------------------------------------------------|----------|
| DECLARATION.....                                      | i        |
| ABSTRACT .....                                        | ii       |
| CONTENTS.....                                         | iii      |
| LIST OF FIGURES .....                                 | v        |
| LIST OF TABLES .....                                  | vi       |
| LIST OF ABBREVIATIONS .....                           | vii      |
| ACKNOWLEDGMENTS .....                                 | viii     |
| DEDICATION.....                                       | ix       |
| CHAPTER ONE: INTRODUCTION .....                       | 1        |
| 1.1 Background .....                                  | 1        |
| 1.2 Problem Statement.....                            | 3        |
| 1.3 Research Objective .....                          | 5        |
| 1.4 Research Questions.....                           | 5        |
| 1.5 Significance of the research.....                 | 6        |
| 1.6 Scope of the research .....                       | 7        |
| CHAPTER 2: LITERATURE REVIEW .....                    | 8        |
| 2.1 Introduction.....                                 | 8        |
| 2.2 Agency theory and corporate governance .....      | 8        |
| 2.3 Executive pay and firm performance.....           | 11       |
| 2.4 Theoretical and conceptual Framework.....         | 18       |
| CHAPTER THREE: METHODOLOGY .....                      | 22       |
| 3.1 Introduction.....                                 | 22       |
| 3.2 Research Design .....                             | 22       |
| 3.3 Population.....                                   | 23       |
| 3.4 Sample and Sampling method .....                  | 25       |
| 3.5 Data Collection methods.....                      | 25       |
| 3.6 Data analysis procedures.....                     | 26       |
| 3.7 Data Analysis.....                                | 27       |
| CHAPTER FOUR: RESULTS AND FINDINGS.....               | 30       |
| 4.1 Introduction.....                                 | 30       |
| 4.2 Directors remuneration and firm performance ..... | 30       |

|                                                   |            |
|---------------------------------------------------|------------|
| 4.2.1 Agricultural .....                          | 30         |
| 4.2.2 Commercial and Services .....               | 37         |
| 4.2.3 Industrial and Allied.....                  | 49         |
| 4.2.4 Finance and Investments.....                | 69         |
| 4.2.5 Alternative Investments.....                | 83         |
| 4.2.6 Analysis for all the companies .....        | 90         |
| 4.3 Common forms of directors pay .....           | 102        |
| 4.4 Key factors that determine executive pay..... | 103        |
| <b>CHAPTER FIVE: DISCUSSIONS, CONCLUSIONS AND</b> |            |
| <b>RECOMMENDATIONS.....</b>                       | <b>106</b> |
| 5.1 Introduction.....                             | 106        |
| 5.2 Discussions .....                             | 106        |
| 5.3 Conclusions.....                              | 110        |
| 5.4 Limitations of the research .....             | 111        |
| 5.5 Recommendations .....                         | 112        |
| <b>BIBLIOGRAPHY .....</b>                         | <b>114</b> |
| <b>APPENDICES .....</b>                           | <b>121</b> |
| APPENDIX ONE: Companies under Study.....          | 121        |
| APPENDIX TWO: Letter of Introduction .....        | 122        |
| APPENDIX THREE: Questionnaire .....               | 123        |

## LIST OF FIGURES

|                                                                                                           |     |
|-----------------------------------------------------------------------------------------------------------|-----|
| Figure 1- Summary concepts.....                                                                           | 21  |
| Figure 2 - Kakuzi remuneration & performance measures .....                                               | 31  |
| Figure 3 - Rea Vipingo – Directors’ remuneration & performance measures .....                             | 32  |
| Figure 4 - Sasini – Directors remuneration & performance measures .....                                   | 33  |
| Figure 5 - Car and General – Directors remuneration & performance measures.....                           | 38  |
| Figure 6 - CMC Holdings – Directors remuneration & performance measures.....                              | 39  |
| Figure 7 - Kenya Airways – Directors remuneration & performance measures .....                            | 40  |
| Figure 8 - Marshalls East Africa – Directors remuneration & performance measures .....                    | 41  |
| Figure 9 - Nation Media Group – Directors remuneration & performance measures.....                        | 42  |
| Figure 10 - Standard Group – Directors remuneration & performance measures.....                           | 43  |
| Figure 11 - TPS Serena – Directors remuneration & performance measures .....                              | 44  |
| Figure 12 - Athi River Mining Company – Directors remuneration & performance measures .....               | 50  |
| Figure 13 - Bamburi Cement – Directors remuneration & performance measures.....                           | 51  |
| Figure 14 - BOC Gases – Directors remuneration & performance measures .....                               | 52  |
| Figure 15 - British American Tobacco – Directors remuneration & performance measures..                    | 53  |
| Figure 16 - Crown Berger- Director’s remuneration & performance measures.....                             | 54  |
| Figure 17 - Mumias Sugar company- Directors remuneration & performance measures.....                      | 55  |
| Figure 18 - East Africa Portland- Directors remuneration & performance measures .....                     | 56  |
| Figure 19 - East African Breweries Limited- Directors remuneration & performance measures .....           | 57  |
| Figure 20 - Kenya Power and Lighting- Directors remuneration & performance measures...                    | 58  |
| Figure 21 - Figure 4.19: Kenya National Oil – Directors remuneration & performance measures .....         | 59  |
| Figure 22 - East African cables – Directors remuneration & performance measures .....                     | 60  |
| Figure 23 - Sameer East Africa– Directors remuneration & performance measures .....                       | 61  |
| Figure 24 - Total Kenya – Directors remuneration & performance measures .....                             | 62  |
| Figure 25 - Unga Group – Directors remuneration & performance measures .....                              | 63  |
| Figure 26 - Barclays Bank – Directors remuneration & performance measures.....                            | 69  |
| Figure 27 - Centum – Directors remuneration & performance measures .....                                  | 70  |
| Figure 28 - Diamond Trust Bank – Directors remuneration & performance measures .....                      | 71  |
| Figure 29 - Housing Finance Company – Directors remuneration & performance measures                       | 72  |
| Figure 30 - Jubilee Insurance – Directors remuneration & performance measures .....                       | 73  |
| Figure 31 - Figure 4.29: Kenya Commercial Bank – Directors remuneration & performance measures .....      | 74  |
| Figure 32 - National Bank of Kenya – Directors remuneration & performance measures .....                  | 75  |
| Figure 33 - Figure 4.31: National Industrial Credit – Directors remuneration & performance measures ..... | 76  |
| Figure 34 - Figure 4.32: Pan Africa Insurance – Directors remuneration & performance measures .....       | 77  |
| Figure 35 - Standard Chartered bank – Directors remuneration & performance measures.....                  | 78  |
| Figure 36 - Express Kenya – Directors remuneration & performance measures .....                           | 83  |
| Figure 37 - Kapchorua Tea – Directors remuneration & performance measures.....                            | 84  |
| Figure 38 - Williamson Tea – Directors remuneration & performance measures.....                           | 86  |
| Figure 39 - Respondents by Sector.....                                                                    | 102 |

## LIST OF TABLES

|                                                                                           |     |
|-------------------------------------------------------------------------------------------|-----|
| Table 1 - Summary Remuneration & Firm Performance – Agricultural sector .....             | 34  |
| Table 2 - Annual remuneration and firm performance for agricultural sector .....          | 34  |
| Table 3 - Individual company regression results - Agricultural sector .....               | 35  |
| Table 4 - Summary Regression – Agricultural sector .....                                  | 36  |
| Table 5 - Summary Remuneration and Firm Performance – Commercial & Services .....         | 45  |
| Table 6 - Annual remuneration and firm performance - Commercial and services sector.....  | 46  |
| Table 7 - Companies regression results- Commercial & Services .....                       | 47  |
| Table 8 - Summary Regression – Commercial and Services .....                              | 48  |
| Table 9 - Summary Remuneration and Firm Performance – Industrial & Allied .....           | 64  |
| Table 10 - Annual remuneration and firm performance for Industrial and allied sector..... | 65  |
| Table 11 - Individual companies’ regression - Industrial and Allied .....                 | 66  |
| Table 12 Summary Regression – Industrial and Allied.....                                  | 68  |
| Table 13 - Summary Remuneration and Firm Performance – Finance & Investment .....         | 79  |
| Table 14 - Annual remuneration and firm performance for Finance and Investment sector...  | 80  |
| Table 15 - Summary regression results for companies -Finance & Investment.....            | 80  |
| Table 16 - Summary regression – Finance and Investments .....                             | 82  |
| Table 17 - Summary Remuneration and Firm Performance – Alternative investments.....       | 87  |
| Table 18 - Annual remuneration and firm performance for Alternative Investments .....     | 87  |
| Table 19 - Individual companies regression results - Alternative Investment .....         | 88  |
| Table 20 - Summary regression results – Alternative Investments .....                     | 88  |
| Table 21 - Remuneration and firm performance for the entire stock Market.....             | 90  |
| Table 22 - Summary regression results – All the companies .....                           | 90  |
| Table 23 - Remuneration, Revenue, Total Assets and Total equity .....                     | 91  |
| Table 24 - Average Remuneration by sector (sh.m).....                                     | 92  |
| Table 25 - Average Revenue Growth by sector .....                                         | 92  |
| Table 26 - Average Net Profit Margin by Sector .....                                      | 92  |
| Table 27 - Average Return on Investment by Sector .....                                   | 93  |
| Table 28 Average Return on Equity by Sector.....                                          | 93  |
| Table 29 - Average Share Price Growth by sector .....                                     | 94  |
| Table 30 - Average Earnings per Share by sector (sh.) .....                               | 94  |
| Table 31 - Remuneration Vs Firm performance - summary.....                                | 95  |
| Table 32 - Remuneration as a percentage of revenue- Agriculture .....                     | 98  |
| Table 33 - Remuneration as a percentage of revenue- Commercial & Services .....           | 98  |
| Table 34 - Remuneration as a percentage of revenue- Industrial & Allied .....             | 99  |
| Table 35 - Remuneration as a percentage of revenue- Finance & Investment .....            | 100 |
| Table 36 - Remuneration as a percentage of revenue- Alternative Investment.....           | 100 |
| Table 37 - Respondents by Sector .....                                                    | 102 |
| Table 38 - Common forms of payment by sector .....                                        | 103 |
| Table 39 - Factors considered in determining director’s remuneration.....                 | 104 |
| Table 40 - Ranking of important factors in determining executive pay .....                | 104 |

## **LIST OF ABBREVIATIONS**

AGM – Annual General Meeting

ANOVA – Analysis of Variance

BAT- British American Tobacco

CEO – Chief Executive Officer

CMA – Capital Markets Authority

DW – Durbin Watson

EABL- East African Breweries Limited

EPS – Earnings Per Share

IAS – International Accounting Standards

IASB- International Accounting Standards Board

ICPAK – Institute of Certified Public Accountants of Kenya

IFRS – International Financial Reporting Standards

KCB- Kenya Commercial Bank

NBK – National Bank of Kenya

NPM – Net Profit Margin

NSE – Nairobi Stock Exchange

OECD – Organization of Economic Cooperation and Development

PWC – Price Waterhouse Coopers

REV – Revenue

ROE- Return on Equity

ROI – Return on Investment

SPG – Share Price Growth

UK – United Kingdom

US – United States

## ACKNOWLEDGMENTS

I would like to thank God for His grace and for being the main source of success in the completion of this thesis. Though I am not able to mention all individuals, I am very grateful for all the help and contributions from everyone (colleagues, respondents to questionnaires and my fellow classmates). Many thanks specifically to the following:

1. My Supervisor Dr. X. N. Iraki for his sacrifice, patience, devotion and valuable advice. It has been a great learning experience under his supervision.
2. Dr. Jim B. McFie, Dr. Ruth Kiraka, Dr. Ishmael Ateya, Dr. Beatrice Dimba and Mr. David Wangombe for their valuable advice, informative guidance, suggestions and other important sources of information.
3. Dr. Silas Onyango, Mrs Rachel Mbogo, Mrs. Beatrice Njeru and Mr. Destaings Nyongesa for their guidance on data analysis and editing.
4. Mr. Evans Mulera (formerly of ICPAK), Mr Zachary Ocheing (CMA-Library), and Mr Vincent Chibini (Strathmore University-Library), for providing data and other information.

## **DEDICATION**

*To God, for His unending graces and to my mother Alice, wife Florence and my two sons Arnold and Aidan, for their unquestionable love that always inspires me.*

## CHAPTER ONE: INTRODUCTION

The first part of this chapter provides a background to the study. This is followed by the research problem, objectives, questions, significance and finally the scope of the study.

### 1.1 Background

Directors' remuneration<sup>1</sup> has been a major area of discussion and debate in several countries including the US (Rosen, 1992; Murphy, 1999; Gibbons and Waldman, 1999), Europe (Eichholtz, Kok and Otten, 2008; Anderson, Banker and Ravindran, 2000) and lately in Asia (Chaudhri, 2003; Kato and Long, 2006; Chan, 2008). Directors' remuneration is sensitive especially where it is perceived that the directors are being paid more than they deserve and to the detriment of a company (Hill, 2006). Excessive pay to directors, fraud and manipulation of financial statements are in various cases cited as factors that contribute to the collapse of companies like in the cases of Enron, WorldCom and Parmalat (Hill, 2006).

Directors are appointed by shareholders to act on their behalf as, it may not be possible for all the shareholders to take part in the management process. According to the agency theory this appointment has led to the principal – agent relationship and subsequently the agency problem (Jensen and Meckling, 1976; Bebchuk and Fried, 2003). The directors act as agents of the shareholders. The agency problem arises when they benefit from the company at the expense of the shareholders (Jensen and Meckling, 1976). The directors benefit by designing remuneration packages where they award themselves high salaries and other benefits that may be very costly to the business and reduce profits that are available for distribution to the shareholders (Jensen and Meckling, 1976). Furthermore directors are in a strategic position in the organization structure to influence their pay (Bratton, 2005). Bebchuk and Fried (2003) argue that if not well structured, the executive compensation will actually contribute to the agency problem.

There are various proposals to resolve the agency problem. Most of the proposals are in a set of corporate governance principles that companies are encouraged to apply, and in some countries, they are enforced through legislation. One of the proposals in

---

<sup>1</sup> Directors' remuneration is also referred to as executive remuneration in this paper

the corporate governance principles is that companies are supposed to appoint a remuneration committee that should be in charge of designing the executive pay for the firm (OECD, 1999; Main, Jackson, Pymm and Wright, 2008). In designing the executive pay, the remuneration committee is supposed to base the executive pay on firm performance (Bebchuk and Fried, 2004). The main objective of this approach is to align directors' interests to those of the shareholders. If executive compensation is based on firm performance, then it is expected that directors will be motivated to perform well and therefore increase their own payment while at the same time shareholders benefit (Bebchuk and Fried, 2004).

However, various studies have criticised and argued against basing executive remuneration on firm performance. The first problem is in measuring firm performance (Rosen, 1992). This is because several factors contribute to firm performance and they arise from sources internal and sources external to the company (Rosen, 1992). The other problem is identifying the main parameters of performance. Kaplan and Norton (1992) argue that businesses tend to lay emphasis on quantitative performance measurement metrics, while qualitative factors like customer satisfaction and innovation are also equally important areas of analyzing firm performance.

Kerin (2003) also argues that firms must have a balance between fixed and variable pay to executives. A fixed pay ensures that whether the firm performs well or not, the directors have provided services to the company. Furthermore the directors assume additional risk in relation to management of the firm when they decide to act as agents for shareholders (Jensen and Meckling, 1976, Jensen and Murphy, 1990b). The variable component is the amount that should relate to performance for example bonuses, profit sharing and options. However additional studies have shown there should be other factors apart from performance that should be considered in determining executive pay. Such factors include experience, age and qualification so that firms can also hire the services of talented executives (Combs and Skill, 2003).

High executive pay is not only due to the agency problem but also greed by executives and weak governance by shareholders (Akst, 2006). However executive pay can be used successfully to not only attract competent executives but also

improve the performance of the firm. The debate on executive pay is expected to continue.

## **1.2 Problem Statement**

Investors consider several factors when making investment decisions. One of the important factors is firm performance (Brown and Reilly, 2009) which is generally measured in terms of profits and returns to investors in the form of share price growth (Brown and Reilly, 2009:6).

Bhagat and Bolton (2008) explain that corporate governance practices improve firm performance. Some of the recommendations regarding corporate governance cover executive appointment, board composition, executive remuneration, communication to shareholders and other stakeholders and board committees (OECD, 1999). In relation to executive remuneration and board committees, companies are encouraged to appoint a remuneration committee that considers among other things firm performance in designing executive remuneration (Fama, 1980; Conlon & parks, 1988; OECD, 1999). Combs and Skill (2003) argue that in addition to firm performance, remuneration committees should consider the director's experience, age and qualifications (academic and professional). This is supported by prior findings by Hogan and McPheters (1980) who studied top 45 executives in US and found a significant positive relationship between executive remuneration and firm performance, experience and age.

Most of the studies on firm performance have focussed on companies in developed countries such as the US, some European countries (Spain and Germany) and Asia. Some studies carried out show a strong positive relationship between executive pay and firm performance i.e. executive pay increases with an improved firm performance while it reduces when performance declines (Joskow and Rose, 1994; Kubo, 2001; Kato and Long, 2006; Buck, Liu and Skovorada, 2008). Other studies show a weak positive relationship between executive remuneration and firm performance (Kubo, 2001; Hassan, Christopher and Evans, 2003; Ozkan, 2007). Other studies have found a negative but weak relationship (Kubo, 2005). Boyd (1996) carried out a research on US firms and his study summarized key determinants of executive pay in addition to

experience, age, qualification and tax as firm size, firm profitability, equity ownership by directors, and resource richness of the board. Other studies also found that firm size is the key determinant of executive remuneration (Aditya, Debashish and Krishnakumar, 2006). In Spain, Crespi – Cladera and Gispert (2003) found a positive relationship between board remuneration and company performance. Other studies have found no relationship between Executive pay and firm performance (Kubo, 2005). In a rare study Brick, Palmon and Wald (2005) showed that there is a link between underperformance and excessive executive remuneration, which partially supports Berchuk and Fried (2003) that high executive compensation may be counterproductive.

In Kenya, issues regarding executive pay have not been debated and are not a source of major headlines unlike in other developed countries<sup>2</sup>. Kenya being a developing country<sup>3</sup> is also considered to be an emerging market (Hoskisson, Eden, Lau and Wright, 2000). Hoskisson et al explain that in an emerging economy, institutional framework to support market based systems are either not available or are very weak and therefore there are very high costs of obtaining information for monitoring corporations. Political and corporate governance structures tend to be weak and these impede on achieving faster economic growth. However, opportunities for economic growth are many.

Locally, Pricewaterhouse Coopers carried out a survey in 2007 on Chief Executive Officers' salaries. The survey showed that the salaries are on the increase with the highest earning CEO earning a base salary of Ksh.2.53 million per month in 2007. This study focused on highest and lowest pays and key Management personnel. Authors who have carried out the studies on firm performance have drawn different conclusions which may be due to regional differences (national, economic and legal).

---

<sup>2</sup> The only latest information available to the author is the survey carried out by PWC discussed in the paper later

<sup>3</sup> Hoskon et al have listed Kenya among the countries considered to be emerging economies. In addition the American mathematical society on <http://www.ams.org/membership/develop.html> (Accessed on 11th March 2010 and also by World trade organization on [http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/org6\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm) (Accessed on 11th March) have listed Kenya as a developing country.

Based on the above discussions the main problem that this study focused on is derived on the principal agent relationship. If the directors of companies listed on the NSE do not base their pay on the performance of the companies, then they may be benefiting at the expense of the shareholders.

The study therefore determined the relationship between executive pay and firm performance for companies listed on the Nairobi Stock Exchange in line with current trends in corporate governance relating to directors remuneration. Furthermore, the study examined the key components of executive pay and also the factors that determine executive pay. The study provides empirical evidence on the status of executive remuneration for companies listed on the NSE.

### **1.3 Research Objective**

The main objective of the study was to establish whether there is a relationship between executive pay and firm performance for NSE companies.

The specific objectives are, to:

1. Determine the relationship between firm performance and executive pay.
2. Establish the main components of executive pay by companies listed on the Nairobi Stock Exchange companies.
3. Determine the important factors that are considered in designing executive pay for companies listed on the NSE.

### **1.4 Research Questions**

The research questions are based on the objectives.

1. Is there a relationship between directors' pay and firm performance?

This question is also given in the form of the null hypothesis:

**H<sub>0</sub>: There is no strong positive relationship between executive remuneration and firm performance**

2. What are the main methods of paying directors?
3. What are the important factors that determine directors pay?

## **1.5 Significance of the research**

The study is of relevance to the following:

### **Investors**

A well functioning stock market is a prerequisite for economic growth (Fischer and Merton, 1985). This is because it avails capital that is essential for businesses. Investors provide capital to companies by purchasing the shares or loan stocks issued by the firms. For investors to provide the capital or loan they consider not only the ability of the firm to pay back the principal but also the return they will get from the firm in the form of interest and dividends. This implies that firm performance is a key consideration of investors (Brown and Reilly, 2009). A firm can adopt several strategies to improve its performance and one of the recommended approaches is basing executive pay to firm performance.

Currently executive pay and firm performance appears to be a sensitive matter especially in developed countries. In Kenya there have been few corporate failures e.g. Uchumi Supermarket (a quoted company). But the subject of executive pay does not concern investors. The study provides an important framework for investors to consider executive pay in firm performance.

### **Firms and remuneration committees**

The study aims at contributing to existing knowledge on executive pay, with major emphasis Kenyan companies. It highlights the current situation on executive pay for local companies and tries to establish whether companies and remuneration committees are complying with current corporate governance practices on remuneration.

### **Regulators**

In addition to local regulators and other professional bodies can use the findings as a reference for policy guidelines (e.g. disclosure) on executive remuneration. The study provides a good foundation for making comparisons between firm performance and executive remuneration and a means of enforcing good corporate practices.

**Academicians and researchers**

Executive remuneration is a major area of discussion and research and the study contributes by providing additional dimensions about executive remuneration in the Kenya. Some issues of interest are highlighted in chapter five on, discussions, conclusions and recommendations.

**1.6 Scope of the research**

The study considered 37 companies listed on the Nairobi Stock Exchange. These are the companies that have been quoted from 2003 up to 2008 and have also provided published financial statements over the same period.

## **CHAPTER 2: LITERATURE REVIEW**

### **2.1 Introduction**

This review is in four parts. The first focuses on the main theories and principles that underlie executive remuneration mainly agency theory and corporate governance. The second part analyses various studies regarding executive remuneration and firm performance. The third part discusses briefly the main features of NSE and the fourth concludes by summarising the theory and key concepts i.e. the theoretical and conceptual framework.

### **2.2 Agency theory and corporate governance**

The agency theory<sup>4</sup> was extensively analyzed by Jensen and Meckling (1976) although its roots can be traced to Smith (1776) and Berle and Means (1932). Smith explained that due to the nature of joint stock companies, where there are many owners (shareholders), directors should be appointed to manage the company on their behalf. The shareholders are referred to as the principals while the directors are the agents. This has resulted to the principal agent relationship although Jensen and Meckling argue that a principal agent relationship arises also in the company when the shareholders borrow and hence the shareholders act as agents of the lenders. However this paper narrows the scope of the principal agency relationship as being that between shareholders and executives.

Smith (1776) explained that even though executives are agents of the shareholders, they are most likely to put their interest first rather than act for the benefit of shareholders. This is what Smith refers to as the agency problem. Berle and Means (1932) suggest that the agency problem is mainly due to the separation of ownership and control and asymmetric information between shareholders and executives. Due to this information asymmetry, managers may use their discretion to benefit their private interests in a variety of ways. For example, managers may engage in empire building (Williamson, 1964) or fail to distribute excess cash when the firm does not have profitable investment opportunities (Jensen, 1986).

---

<sup>4</sup> Some studies also refer to agency theory as agency problem.

Jensen and Meckling (1976) argue that as a result of the agency problem, the shareholders will have to ensure that the directors are monitored effectively and thus incur agency costs. Zeckhauser and Pound (1990) also explain that if a firm's ownership is highly dispersed (less concentrated), the monitoring process becomes very challenging and costly (i.e. the firm incurs high agency costs).

Several authors for example Ross (1973), Jensen and Meckling (1976) Fama (1980), and Bloom and Milkovich (1998) and the latest one by Cruz, Gomez-Mejia and Becerra (2010) have made contributions towards the agency theory and some of them support the theory although there are different suggestions on how to resolve the problem). However Perrow (1986) criticized the agency theory for being excessively narrow and having few testable implications. He suggests additional research to be carried out to include a range of important issues such as managerial behavior.

The two main approaches recommended to assist in effective monitoring of the board are corporate governance and executive pay linked to performance (Fama and Jensen, 1983; Kosnic, 1987; Pearce, Stevenson and Perry, 1985; Shavell, 1979 and Ungson and Steers 1984).

There is no standard definition of the term corporate governance though some authors have made propositions. Viewing the corporation as a mixture of explicit and implicit contracts, Garvey and Swan (1994) explain that governance normally determines how the firm's top decision makers manage the contracts. Shleifer and Vishny (1997) also explain that corporate governance deals with the ways in which providers of finance to business firms get assurance of a return on their investment. A similar concept is suggested by Caramanolis-Cötelli (1995), who also explains that corporate governance is determined by fair allocation among stakeholders within and outside the business. John and Senbet (1998) propose a more comprehensive definition that corporate governance deals with mechanisms by which stakeholders of a business exercise control over the management and therefore protect their interests. Stakeholders range from shareholders, lenders, employees, customers, suppliers and even the public. According to the Organization for Economic Cooperation and

Development-OECD (1999) corporate governance relates to the internal means by which corporations are operated and controlled.

Bocean and Barbu (2007) explain that good corporate governance is an important step in building market confidence and encouraging more stable, long-term international investment flows. They also explain that many countries see better corporate governance practices as a way to improve economic dynamism and thus enhance overall economic performance. As a result corporate governance principles are now being encouraged and even made mandatory in many countries through legislation. Compliance is enforced by regulators.

Some of the important principles of corporate governance include equitable treatment of all shareholders, enhanced disclosure requirements, communication with the shareholders and an effective board of directors (OECD, 1999). In discharging its duties effectively, the firm has to consider remuneration which should be fair and based on the firm performance.

Some studies carried out to establish the threefold relationship between corporate governance, firm performance and executive pay. Lee, Lev and Yeo (2008) explained that there is a positive association between firm performance and corporate governance such that the firms that have a more effective corporate governance structure tend to perform better than those with a less effective structure. Within the same study, the two authors also found that a good executive compensation package reduces agency costs and improves firm performance. However, Kato and Long(2006) found that in most Chinese companies, corporate governance measures such as independent board do not promote executive pay that is tied to performance.

## **2.3 Executive pay and firm performance**

The current study focused on Kenya as most of the studies have been done in other countries. Several studies have been carried out in the areas of executive pay, how to measure firm performance and whether performance based pay is effective.

Executive pay is the compensation that is paid to the directors when they carry out their management role in the firm (Carola and Saks, 2005). Carola and Saks explain that executive pay has increased over the past two decades, which led to a lot of attention by stakeholders. Bebchuk and Fried (2003) argue that executives are paid excessively such that executive compensation is becoming part of the agency problem rather than a solution. Under the principles of corporate governance by the center of corporate governance (1999), a remuneration committee should be formed to design the executive compensation. In designing the executive remuneration, the remuneration committee will often use the services of management consultants and other experts coupled with market surveys.

Kerin (2003) explains that a good mix of executive pay is one that includes fixed payments, short-term incentives, long-term incentives, entry benefits, exit benefits and non-pecuniary benefits. Fixed payments just like for other employees are those that are unaffected by a firm's performance; they include both basic salary and various fringe benefits (for example health cover, car, and school fees). Short-term incentives involve payments (typically cash bonuses), contingent upon the achievement of one or more short-term (typically annual) targets, such as profit after tax, earnings per share, return on capital employed, return on equity, or more specific targets (such as cost reduction or sales growth). Long-term incentives are inducements to achieve longer term targets (generally related to shareholder value creation over three to five years) and are typically provided through the award of shares and/or options. Entry benefits are payments (sign-on bonuses or 'golden hellos') to induce a potential CEO candidate to accept the position and are typically paid in cash or an award of shares and/or options. Exit benefits are payments made to induce a CEO to leave the firm.

Various special-purpose compensation elements are also offered at times. For example, after a merger or acquisition, retention bonuses (golden handcuffs) are often offered to lock in key executives for a period of time. The last set is non-pecuniary benefits which range from enjoyment of the job and the respect of staff and analysts through to prestige and membership of a club often have more influence on executives' behavior as compared to the other incentives (Kerin 2003). Shavel (1979) argues that the fixed payment is more important than most of the others because the executives assume greater risk when they add control to ownership of a firm.

Conlon and Parks (1988) and Fama (1980) advocate that executive pay should be linked to firm performance. The main justification is that in the long run both the executives and shareholders and by extension other stakeholders will benefit. Combs and Skill (2003), argue that in addition to firm performance, remuneration committees should consider the director's experience, age and qualifications (academic and professional). This is supported by prior findings of Hogan and McPheters (1980) who studied top 45 executives in US and found a significant positive relationship between executive remuneration and firm performance, experience and age. However the authors also found a positive relation between executive remuneration and qualification though the relationship was not significant. Rose and Wolfram (2002) also argue that the remuneration committee should consider tax implications which could play a significant role in the pay based on performance.

Boyd (1996) carried out a research on US firms, and his study summarized key determinants of executive pay apart from the experience, age, qualification and tax. The determinants were firm size, firm profitability, equity ownership by directors, and resource richness of the board. Boyd explained that as expected, executive remuneration is higher for firms with large size, high profits, smaller shareholder concentration and competent board. It appears that his study added the dimension of firm size and equity shareholding as key factors in executive remuneration.

In the public sector, the main approach for ensuring an executive officer performs to the highest expected level is by performance contracting. Performance contracting involves designing the contracts of the officer that ensures some quality measurable

objectives can be achieved and rewards are based on the result (FCS Group, 2005). This is another area of discussion which was outside the scope of the current study.

There are several practical challenges of implementing a compensation scheme that is tied to firm performance. First, Murphy (1997) argues that most firms would want to design executive packages that attract talented executives. Some firms would like to be the best in terms of remuneration. This is also argued by Lazear and Rosen (1981) in their tournament theory where individuals (in this context, executives) compete for promotion and rewards. High performing executives with considerable managerial potential win promotion and get high compensation. Therefore when firms hire executives whether from within or outside, the initial package designed is not based on performance but rather a package that is meant to attract the executives. Lazear and Rosen also argue that when the contract commences, performance becomes an important factor in remuneration. The firms also consider other influences like employee unions, shareholders, regulators and politicians concerns over the executive remuneration.

The second problem that arises in implementing pay based performance is that there is no benchmark against which performance can be evaluated (Gibbons and Murphy, 1990). Several authors have suggested different tools of evaluating performance with the famous one being the balance score card by Kaplan and Norton (1992). In the balance score card, Kaplan and Norton argue that performance should not only be quantitative (financial) but also qualitative (Customer, learning and growth and improvements on internal business processes). Gibbons and Murphy (1990) argue that tools such the balance score card only provide a wider framework of evaluating managerial performance but there is still a lot of subjectivity in awarding the scores.

The third problem is how to measure firm performance. Even though there are several recommended measures, none of these measures seem to be satisfactory (Bacidore, Boquist, Milbourn, and Thakor, 1997)). Rosen (1992) argues that optimal compensation is complicated by various factors one of them being performance measurement. In general there are three categories of studies. Some studies of pay for performance focus on market based measures, mainly being the market price per

share or price earnings ratio (Jensen and Murphy, 1990; Barro and Barro, 1990; Hubbard and Palia, 1994).

Other studies focus on accounting based measures that rely on the firm's financial statements (accounting measures) such as sales growth, profit margins, return on capital employed and others (Antle and Smith, 1986; Lambert and Larcker, 1987). The third category of studies includes a mixture of the two i.e. both accounting and stock market returns (Sloan, 1993; Crespi – Cladera and Gispert, 2003). Sloan argues that a robust measurement of firm performance should incorporate both accounting and stock market returns. Kaplan and Norton (1992) suggest that when measuring the firm performance, financial indicators are not important on their own but additional dimensions of customer focus, learning and innovation should be included.

Hall and Murphy (2003) also explain that it is very challenging to implement pay based on performance especially stock bonuses. The sources of the challenge are mainly from time horizon, creative accounting and management aversion to risk. In the case of time horizon, it is expected that the executives will take decisions that increase shareholders wealth in the long-run. Unfortunately, the pay based performance looks at short-term profits. Creative accounting is where executives tend to report a better financial performance and position than what the true and fair position is. This information is misleading although beneficial to the executives (Peng and Röell, 2008). Hall also argues that majority of the executives are risk avoiders and therefore this may limit the ability of the firm to perform well even if there is a profitable but risky project. Goering and Harikumar (1999) also agree that executive compensation has an influence of investment decision making. Another important challenge in executive pay based on performance is that the executives normally influence their own pay. This is done in several ways but mainly having undue influence on the remuneration committee (Sridharan, 1996).

Finally, studies carried out between executive pay and firm performance show mixed results. An earlier study carried by Joskow and Rose (1994), on US CEO salaries from 1970 to 1990 showed that, CEO pay has a strong positive relationship with firm performance measured by both accounting and market returns. Another study was

carried out by Hassan, Christopher and Evans (2003) in which an analysis of a sample of 100 listed companies in Malaysia was carried out. The study found a positive but weak relationship between Directors' remuneration and firm performance.

Additional studies were carried out by Kubo (2001 and 2005). In the earlier study, Kubo compared the relationship between executive remuneration and firm performance for UK and Japanese firms. He found out that there was a strong positive relationship between executive remuneration and firm performance as measured stock market returns for UK firms, but a weak positive relation for the Japanese firms. The additional study in 2005 was carried on 210 listed companies in Japan using the regression model found a weak negative relationship between executive compensation and firm performance. The first study highlighted that corporate governance factors had played a big role in influencing the outcome.

Kato and Long (2006) also analyzed a sample of companies listed in China and found a strong positive relationship between executive pay and firm performance. The main dimension of their study was to find out how corporate governance practices influence firm performance.

A recent study by Ozkan (2007) seems to contradict that of Kubo (2001). Ozkan analyzed the relationship between executive pay and firm performance for a set of 390 UK companies (except those in the financial sector) quoted on the Financial Times Stock Exchange between 1999 and 2005 and found that even though the relationship was positive, it was weak. The difference is attributable to the population differences.

The latest study was that carried out by Buck, Liu and Skovorada (2008) which analyzed a sample of Chinese listed companies and interestingly confirmed the findings in the study of Kato and Long (2006) where the relationship was positive and strong. Furthermore the authors found that firm performance and executive pay mutually affect each other.

Studies carried out in other countries for example Brunello et al. (2001) on Italian data, Randhoy and Nielsen (2002) on Norwegian and Swedish firms did not find any

link between pay and performance. Fernandes (2008) also reaches a similar conclusion based on a sample of Portuguese firms. Finally, Duffheus and Kabir (2007) did a study on Dutch firms and found a negative pay-to-performance relation.

Some studies have also introduced different dimensions to the relationship between firm performance and executive pay. In Spain, Crespi – Cladera and Gispert (2003) studied a sample of large Spanish firms and their results confirm the positive relationship between board remuneration and company performance and the relevance of governance structure in the power of the compensation-performance relationship.

Aditya, Debashish and Krsihnakumar (2006) studied a sample of Indian companies by using a regression model and found that firm size was the key determinant of executive pay. Shah, Javed and Abbas (2009) also studied a sample of 114 companies listed on the Karachi Stock Exchange for the period between 2002 and 2006 and explain that even though there is a positive relationship between executive remuneration and firm performance, it was weak and size was a key determinant of executive pay.

In a rare study, Brick, Palmon and Wald (2005) showed that there is a link between underperformance and excessive executive remuneration, which partially supports Berchuk and Fried (2003) that high executive compensation may be counterproductive.

In Kenya some surveys on salaries have been done the most recent being a survey by PriceWaterhouseCoopers (PWC) in 2007. The survey showed that it would cost Sh2.53 million, to hire the top ranked CEO in the financial services sector (the most expensive), up from Sh2.23 million in 2005 (Kwama, 2009). The current survey was carried out in 2007, and covered 123 companies across all sectors of business in the public and private. According to the PWC report, the average cost of employing a CEO in Kenya is Sh1.03 million, while the lowest cost of employing a CEO was recorded in the trade sector, with a median salary of Sh274, 083, which is by 58 per lower than Sh434, 202 per month in 2005.

Most of the studies have focused on companies in developed countries in US, Europe and Asia and the results have been mixed with some being contradictory. The recent survey of PWC also did not highlight the key components of executive pay, factors that influence the pay and the situation about NSE companies. It also focused on Key management personnel and Chief Executive Officers rather than directors, the focus of this study.

## **2.4 Theoretical and conceptual Framework**

This study was carried out on the basis of the agency theory as per the details given in the literature. As a result of separation of ownership and control, there is always a conflict between executives and shareholders (Jensen and Meckling, 1976). Unless executives are regulated, they will tend to benefit from the company at the expense of the shareholders. For purpose of this study executives are the directors involved with the management of a company which comprises mainly of the board of directors and may include the chief executive officers.

This study was also based on the background that a vibrant stock market is essential for economic growth (Fischer and Merton, 1985). For investors to gain confidence in providing capital to a firm, then improving firm performance is critical. Even though there are many approaches to improving firm performance, good corporate governance practices are vital.

The study is also in agreement with the fact that one of the good corporate governance practices is basing executive pay to firm performance (OECD, 1999). This will ensure that both executives and the shareholders benefit. The Capital Markets Authority in Kenya requires companies listed on the Nairobi Stock Exchange to comply with the corporate governance principles. Therefore the study expected a strong positive relationship between executive remuneration and firm performance.

Executive remuneration includes all benefits to executives made up of fixed payments, short-term incentives, long-term incentives, entry benefits exit benefits and non pecuniary benefits (Kerin, 2003). The main components were to be determined from the study. The study also expected bonuses and stock options to be the common forms of executive remuneration and firm performance to be a key determinant of executive remuneration.

Measuring firm performance is controversial as evidenced by several studies explained shortly. Neuman (2006) recommends that where a key variable can have several indicators, then using multiple indicators of the same variable increases the reliability of the main indicator. Therefore to ensure the study is strong several firm

performance indicators were used. The major indicators were Revenue Growth, Net Profit Margin, Return on Investments, Return on Equity, Earnings per Share and changes in share price (Share Price Growth).

Kato and Long (2006) used Revenue Growth as one of the performance indicators in their study which is determined by comparing revenue from one financial period to the next. Though not a good indicator of firm performance, revenue growth raises chances of making future profits where operating costs are well controlled. Revenue is also considered to be a good estimate of the market share when it is compared with other firms in the same industry. However care should be taken when using revenue growth because it is subject to manipulation by the firm (Ross, Westerfield and Jaffe, 2008). For firms in finance and investment, revenue is interest income (banks), gross premium (insurance companies), and administration fees or investment income (investment firms).

Brunello (1997), Kubo (2005) and Duffheus and Kabir (2007), used the Net Profit Margin in their studies. Gitman (2003) argues that Net Profit Margin is one of the best profitability ratios that can be used in assessing firm performance. It is taken as net profit after tax divided by revenue. It measures the return a firm generates in relation to one unit of sales and the ability of the firm to control its operating costs. An increase from one period to the next is a good sign for the firm (Gitman, 2003: 64).

Kato and Long (2006), Duffheus and Kabir (2007) and Buck, Liu and Skovoroda, (2008) used return on Investment or total assets also as a measure of firm performance in their studies. Return on Investment or total assets measures the ability of the firm to generate a return on all the available resources. It is computed as the Profit after tax divided by total assets. This is also a good measure of performance as it tries to justify the use of resources by the firm (Gitman, 2003:65).

Kubo (2005) used Return on Equity as one of the measures of firm performance as it measures the return that shareholders of a firm will get (Watson and Head, 2007: 52). It can also be described as the measuring earnings power of shareholders book value of investment (Van Horne and Wachowitz, 2001:155). It is computed by dividing profit after tax with owners' equity (shareholders funds).

An interesting observation from all these studies is that none of them used Earnings per Share. Earnings per Share measures the return in currency expected on one share of a company (McLaney, 2006:57). It is computed by dividing profit after tax with the average number of ordinary shares outstanding throughout the financial period (McLaney, 2006:57). It is a very important investor ratio and it is normally assumed that apart from market fundamentals, investors base their decision making on this ratio. The current study included Earnings per Share as a performance indicator as the author believes that it does not in any way reduce the quality of the analysis.

Joskow and Rose (1994), Kubo (2001), Fernandes (2005), Kato and Long (2006), Duffheus and Kabir (2007) and Buck, Liu and Skovoroda, (2008) all used a change in stock market price (Share Price Growth) as a performance indicator in their studies. A change in share stock price is a good stock market indicator of firm performance (Brown and Reilly, 2009). This is because an increase in the stock price leads to a capital gain for an investor. However, it is argued that stock price changes are affected by many variables not limited to firm performance (Brown and Reilly, 2009).

As discussed in the literature Kaplan and Norton (1992) recommend the use of both financial and non financial factors in evaluating firm performance. This study could not consider qualitative factors such as customer, learning and growth and improvements on internal business processes because of the limited access to such information which is normally part of the internal management reports (Kaplan and Norton, 1992).

The following diagram summarises some of the ideas covered in the literature.

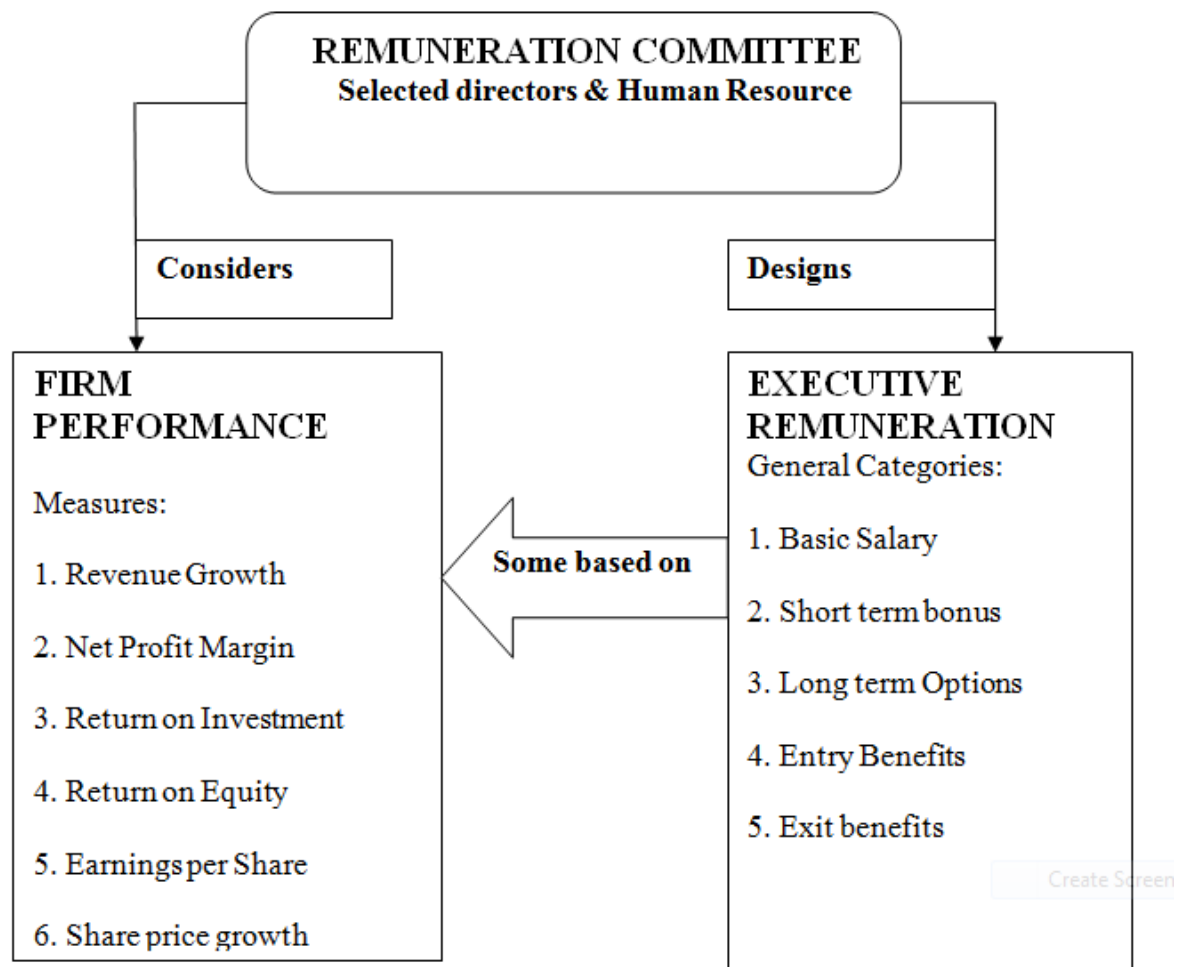


Figure 1- Summary concepts

## **CHAPTER THREE: METHODOLOGY**

### **3.1 Introduction**

This chapter provides the methods that were used to address the objectives and research questions. It also provides the research design, the target population, sample and sampling methods data collection methods and procedures, and finally data analysis procedures.

### **3.2 Research Design**

This study was both quantitative and qualitative (Neuman, 2006). In establishing the relationship between executive remuneration and firm performance, a quantitative analysis of the financial information was done. This approach is justified on the basis that it is easier to measure the remuneration and performance variables. The study was also qualitative because qualitative data was analysed in establishing the common forms of executive remuneration and factors that determine firm performance. The justification for using both quantitative and qualitative approaches is to be able to enhance the reliability of the findings and identify any inconsistencies (Neuman, 2006: 196).

The main method of data collection was through reference to the company's financial statements that are available from several sources (but mainly from the companies' offices) to study the pay and performance relationship. The share prices of companies was also available from the press (main source was the Daily Nation and the Nairobi Stock exchange 2002 and 2008 Handbooks). To establish the main components of executive pay and challenges of pay for performance schemes, a self administered questionnaire was used. However this was supplemented by a follow up visit to help get responses for the questionnaires where there was no response or where data was incomplete.

The study was also cross sectional and longitudinal. In establishing the relationship between executive pay and firm performance, a firm's financial performance and share price was analysed from the years 2003 up to 2008. The main justification for this period is because the Capital Markets Authority issued proposals for good

corporate governance in 2002 (CMA Handbook, 2002). The firms were also analysed during this period being the latest to establish the current position about executive pay and firm performance. The time period is chosen because of availability of data financial statements and recommendation of corporate governance. Furthermore, the firms were analysed to establish whether there was relationship between remuneration and firm size as measured by Revenue, Total assets and Total Equity.

### **3.3 Population**

The main population was the companies listed on NSE due to the fact that companies listed on the NSE are required to comply with corporate governance rules (CMA, 2002).

The NSE was set up in 1954 and was made up of stock brokers operating on a voluntary basis (NSE Handbook, 2002). There is no much information about its activities prior to Kenya's independence in 1963, but there has been a rapid growth in trading. This is attributable to various companies trying to raise share capital and the privatization of various companies and banks by the government of Kenya.

As at December 2008 there were 58 listed companies (NSE Handbook, 2008) although 3 companies had their trading suspended i.e. Hutchings Biemer Ltd, Uchumi Supermarket Limited and Carbacid Investments Ltd. The listed companies are classified into three main categories i.e. The Main Investment Market (with has four categories, Agricultural, Commercial and Services, Finance and investments and industrial and allied), the Alternative Investment Market and the Fixed Income Sector.

Only 37 companies (see appendix one) under the Main Investment Market and Alternative Investment market were considered. The remaining 21 companies were excluded from the study because some were not listed during the entire period under consideration (for example Safaricom, Kengen and Cooperative bank), either annual reports were not available (for example Baumann), or there were changes in the structure and reporting (for example CFC Stanbic) and others were suspended from listing. Appendix one shows the companies analyzed and the nature

of their business as analyzed from the relevant annual reports of directors, the chairman's or Chief Executive Officer's (CEO).

The companies quoted on the Nairobi Stock Exchange have several sources of regulation. The main sources of regulation includes the Nairobi Stock Exchange listing and reporting requirements, the Capital Markets Authority, the Companies' Act and financial reporting requirements by the Institute of Certified Public Accountants of Kenya (ICPAK). For the purpose of this study the important regulations are those that require listed firms to prepare annual reports and present these to the members at the AGM (CA 1962). These financial statements provide information about the accounting performance and executive remuneration.

In addition, the Nairobi Stock Exchange prepares handbooks (2002 and 2008) and other information that is published in the press about the market price of the companies' shares and hence assists in evaluating stock market performance. The Capital Market Authority (CMA, 2002b) provides guidelines on good corporate governance practices part of which require listed companies to constitute a remuneration committee that designs the directors' remuneration which should be based on firm performance.

Companies listed on the NSE prepare their financial statements in accordance with the requirements of the Companies Act and International Financial Reporting Standards (IFRSs). The IFRSs are developed by the International Accounting Standards Board (IASB) but enforced locally by ICPAK. The relevant accounting standards are mainly International Accounting Standards (IAS) No. 1 'Presentation of financial statements' and IAS 24 'Related parties' (IASB, 2009).

The Companies Act provides disclosure requirements part of which requires firms to provide information about directors' remuneration. Unlike comprehensive disclosures in other countries like the UK and US, Nairobi Stock Exchange companies provide a consolidated figure for directors' remuneration only making a distinction between fees and other emoluments. In addition, the consolidated figure includes a component of non executive directors' fees and remuneration which is assumed not to be a significant component of the entire remuneration.

### **3.4 Sample and Sampling method**

As explained in the literature the main objective was to use all the 58 listed companies therefore eliminating the need to sample. However the companies had to be narrowed down to 37 companies.

### **3.5 Data Collection methods**

In order to find out directors remuneration, the main source of information was the financial statements of the companies that are published annually. These are considered to be secondary sources of information. A quoted company is required to submit a copy of its annual returns to regulators like the Capital Markets Authority. Some financial statements are also available on-line. Frankfort-Nachmias and Nachmias (1996) explain that secondary sources of data are considered to have several weaknesses such as their being approximates, having limited access to and the reliability of the collection procedures. They also explain that secondary data can be used if it is the only possible way of addressing a given objective in a study. Therefore the use of financial statements in the current study as a mode of secondary data is more justified on the basis that it is the only reliable means of measuring the relationship between executive remuneration and firm performance. It is important to note that the information from the financial statements was structured to enable address the objectives of the study.

In order to determine the main forms of directors' remuneration, the main sources of primary data were the responses to the questionnaires. The questionnaires were used in order to get structured responses and for ease of analysis as opposed to other methods. (Gill and Johnson, 2002:115). The questions were structured to meet the specific objectives in order to improve the response rate (Gill and Johnson, 2002: 115). Kothari (2006) recommends the use of questionnaires where the respondents are senior management as they may have limited time for interviews. The respondents were mainly members of a remuneration committee (composed of selected directors, Finance officers and Human resources). The questionnaires were self administered,

but with a follow up mainly through a visit. The main challenge considered was the lack of cooperation from senior management of the companies, due to time or a none response policy. Some respondents explained that they were not comfortable providing the information about their directors. However they provided the information with the clarification on confidentiality and when the contextual background was provided (Newman, 2006:284). To improve reliability and chances of success on the questionnaires a pretesting procedure was carried out on several management personnel and this also helped to determine relevant questions (Newman, 2006:286). Most of the respondents preferred closed questions but there was room to accommodate additional comments.

Finally, the data from the financial statements was collected at the same time the questionnaires were issued.

### **3.6 Data analysis procedures**

The financial statements were analyzed and financial information on the Directors' Remuneration, Revenue, Net profit (profit after tax), Total assets and Total equity summarised. Other ratios already provided in the financial statements like Earnings per Share were also summarized. Thereafter the remaining ratios were computed based on the formulas given in the literature.

From the questionnaires, the response rate was about 62% (23 companies out of 37 companies). Initially, out of the 37 questionnaires sent to selected individuals in the remuneration committee, only 10 were filled and sent back. For the other 13 companies, a follow up visit was made close to two weeks to a month for them to provide feedback. Eight respondents across all sectors explained that they operate a no response policy and the remainder (6) did not want to be involved in the study and gave no feedback. No response was received from the Alternative Investment sector companies of the NSE.

### **3.7 Data Analysis**

Regression was the main tool of analysing the relationship between executive remuneration and firm performance. This is because regression is the most suitable tool to use in studying relations between variables (Jonson and Kuby, 2007:713; Triola, 2001:538; Weiss, 2001:682). As opposed to an alternative method i.e. covariance, regression is able to provide not only the relationship between two or more variables (whether it is positive or negative) but also provides information about the strength of the relationship (Jonson and Kuby, 2007). Covariance analysis only gives a general sense of direction whether it is positive or negative (Jonson and Kuby, 2007:697). Furthermore covariance cannot be used where there are many variables.

To establish the relationship between executive pay and firm performance, the strength of the relationship for individual companies, the sector and the entire stock exchange, the simple regression was used. The simple regression was preferred because there were few data items (number of years is only six). Even though multiple regression could have been used at the sectoral level, the nature of the performance variables tended to report a high multicollinearity. Multicollinearity arises when the independent variables correlate with each other such that the regression equation cannot be relied upon (Defusco, Mcleavy, Pinto and Runkle, 2001). Multiple regressions carried out at the sectoral level confirmed multicollinearity because the variables had high Variance Inflation Factors (VIF). But at the multiple regression that was carried out on the entire stock market had a lower variance inflation factor. Even though correcting for multicollinearity requires a variable to be removed from the equation (Defusco et al, 2001), the purpose of this study was not to develop a regression equation for executive remuneration and firm performance but to establish the nature of the relationship. Furthermore removing some of the variables makes the study less robust.

Apart from multicollinearity, an additional problem that was expected to arise was the serial correlation or autocorrelation. Autocorrelation arises when regression errors are correlated across observations, and therefore, the important measures such that the standard errors limit the usefulness of the analysis of variance (Defusco et al, 2001).

Auto correlation can be checked using the Durbin Watson (DW) Statistic which generally highlights a possible positive serial correlation if the value is significantly below 2, and a negative serial correlation if the DW is significantly higher than 2 (Defusco et al, 2001). The level of serial correlation is also based on the number of observations and the number of independent variables.

The executive remuneration was regressed with each of the six firm performance variables by using data from each company for each of the six years. The regression was done first for each company, then at the sector level and then finally the entire stock market. The simple regression equations were given as follows:

$$\text{REM (Ksh.m)} = \alpha + \beta \text{ REV GR (\%)} + \varepsilon$$

$$\text{REM (Ksh.m)} = \alpha + \beta \text{ NPM (\%)} + \varepsilon$$

$$\text{REM (Ksh.m)} = \alpha + \beta \text{ ROI (\%)} + \varepsilon$$

$$\text{REM (Ksh.m)} = \alpha + \beta \text{ ROE (\%)} + \varepsilon$$

$$\text{REM (Ksh.m)} = \alpha + \beta \text{ EPS (sh.)} + \varepsilon$$

$$\text{REM (Ksh.m)} = \alpha + \beta \text{ SPG (\%)} + \varepsilon$$

REM is directors' remuneration and REV GR, NPM, ROI, ROE, EPS and SPG being the Revenue Growth, Net Profit Margin, Return on Investments, Return on Equity, Earnings per Share and Share Price Growth respectively. Alpha ( $\alpha$ ) is the fixed component of the executive pay while beta ( $\beta$ ) is the component that depicts the relationship between the executive pay and the performance measures and  $\varepsilon$  is the error term. The main focus was on the beta ( $\beta$ ). The regression analysis was carried out using the Minitab version 14 that provided useful information for analysis of variance.

As explained in the methodology, the study expected a strong positive relationship between executive pay and firm performance as measured by the various performance indicators. The main null hypothesis tested in the study was given as follows:

**H<sub>0</sub>: There is no strong positive relationship between executive remuneration and firm performance**

From the regression equations an analysis of variance (ANOVA) was used to explain the nature of the relationship between executive pay and firm performance and also the strength and significance. The nature of the relationship (i.e. whether it is positive or negative) is indicated by the sign before  $\beta$  in the equation. For example a  $+$   $\beta$  means the relation is positive and a  $-$   $\beta$  means the relationship is negative. The significance of the relationship is indicated by various measures such as the coefficient of determination ( $R^2$ ) and the P Value.

An important point to remember here is that in order to rank companies in order of payment of directors' remuneration, the study expressed directors' remuneration as a percentage of revenue rather than trying to determine amount per director. As mentioned on the limitation of the study the information available is inconclusive to allow for computing an amount per director.

Finally, data collected from the questionnaires was coded and classified and thereafter counted for the purpose of ranking the main forms of directors' remuneration and the important factors that determine this pay.

## **CHAPTER FOUR: RESULTS AND FINDINGS**

### **4.1 Introduction**

The results and findings have been presented in six parts. The first five present the results of each company over six years from 2003 up to 2008. The companies are classified in each sector, i.e. Agricultural, Commercial and Services, Industrial and Allied, Finance and Investments and finally Alternative Investments. Each of the first five parts also summarises results for each sector. The last section presents the combined results for all the companies over the six years. Part of the discussion is also presented in each section but the main findings are explained in chapter five.

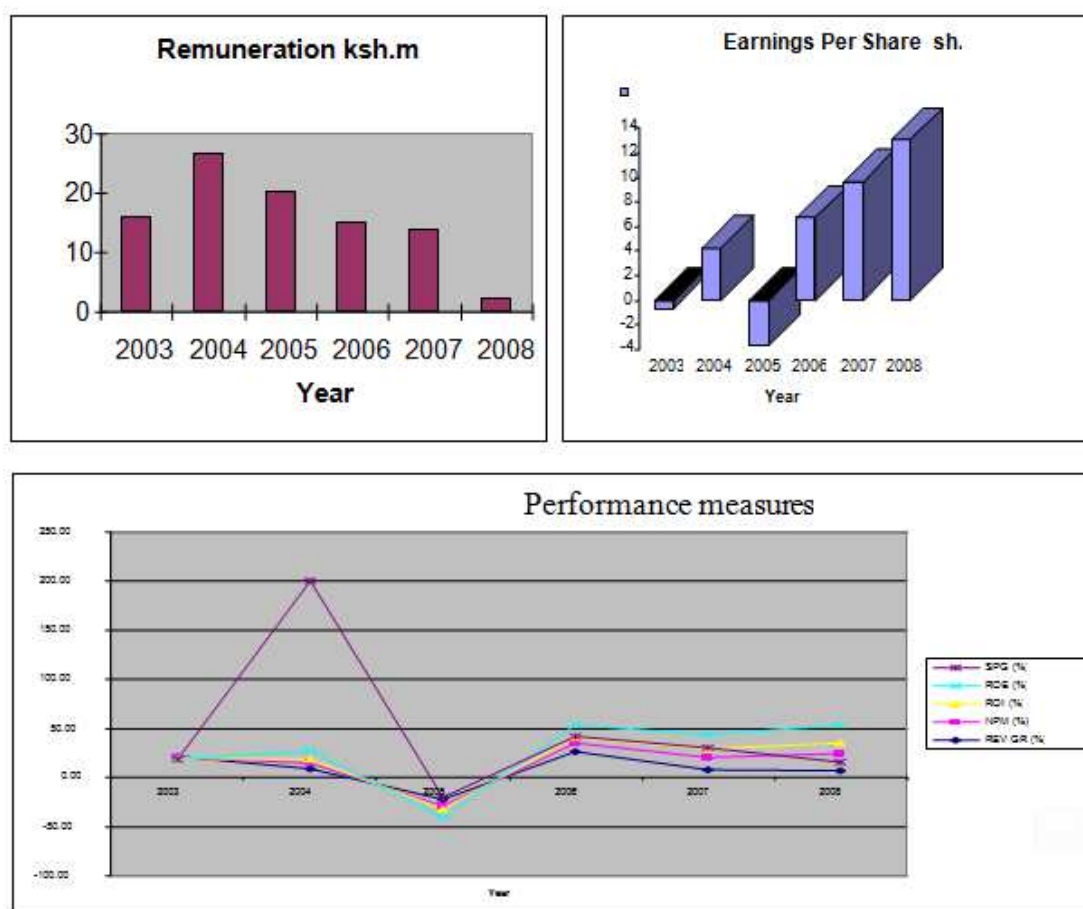
### **4.2 Directors remuneration and firm performance**

#### **4.2.1 Agricultural**

Apart from Kakuzi, most of the firms in the Agricultural sector reported an average increase in executive remuneration over the six years. In contrast to the Earnings per share of Kakuzi showed an improvement over the period with others showing little change (Rea Vipingo). All the other performance indicators did not show any improvement apart from the share price which had an exceptionally volatile performance. Figures 2 to 4 summarise the patterns in Remuneration, Earnings per Share and firm performance. The regression results for each company over the six years presented varying results with Kakuzi showing a negative relation between remuneration and other performance measures except for share price growth. The rest of the companies in the agricultural sector showed a positive relation.

The summaries of the performance indicators and regression analysis are also given in tables 1 up to 4.

## Kakuzi



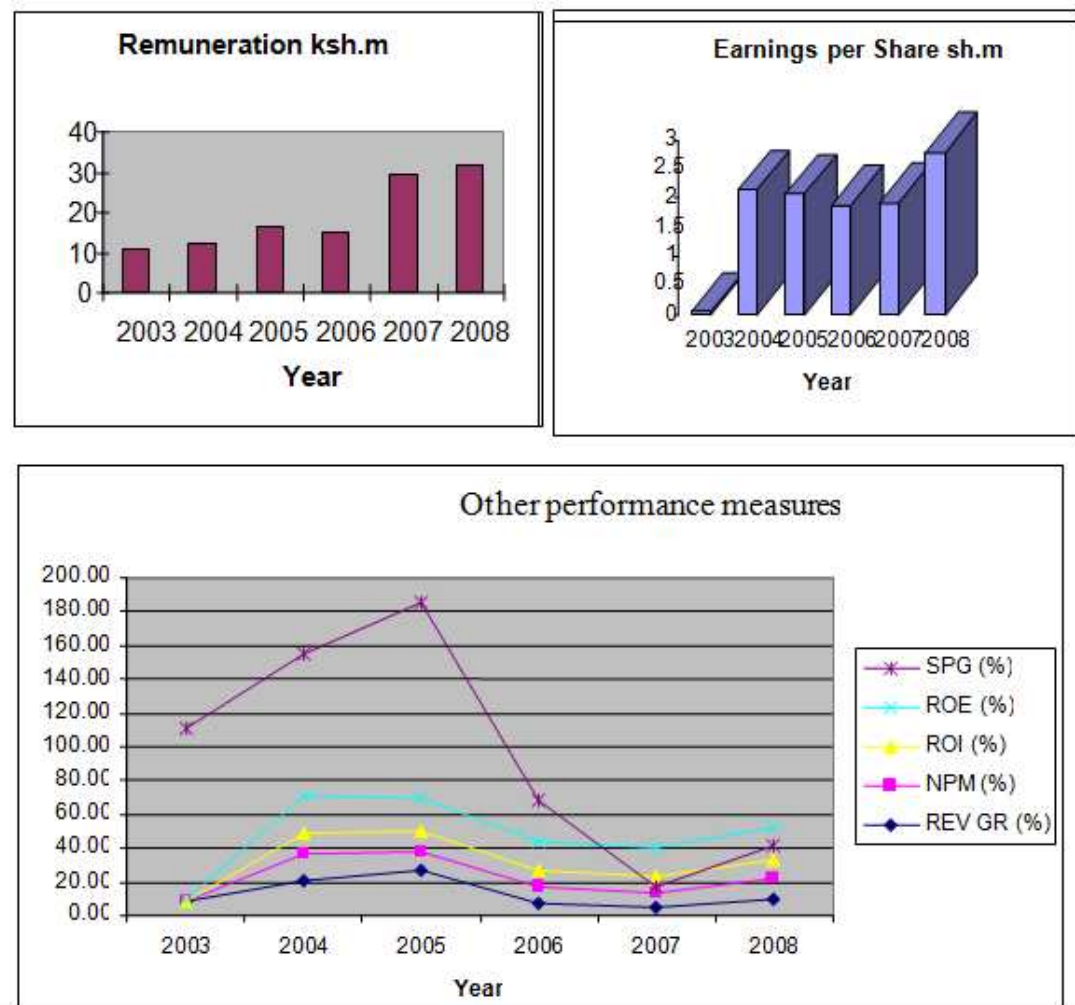
**Figure 2 - Kakuzi remuneration & performance measures**

The remuneration increased in 2004 but declined significantly from 2005 to 2008 with 2008 remuneration being the lowest. The Earnings Per Share declined in 2005 but increased significantly in 2008, with the 2008 Earnings per share being the highest.

Most of the Performance measures had declined in 2005 but improved from 2006 with some stability over the years to 2008. The Share price reported a significant increase in 2004 but came in line with the other measures in 2005.

The initial decline in performance reported in 2005 was attributable to lower coffee production in 2004, significant decline in the market value of biological assets (Plantations) and adverse changes in exchange rates. However, from 2006 performance improved due to Avocado sales and improving tea prices in the global market. There was no explanation of the decline in directors' remuneration despite the fact that the number of directors in Kakuzi remained relatively the same throughout the period.

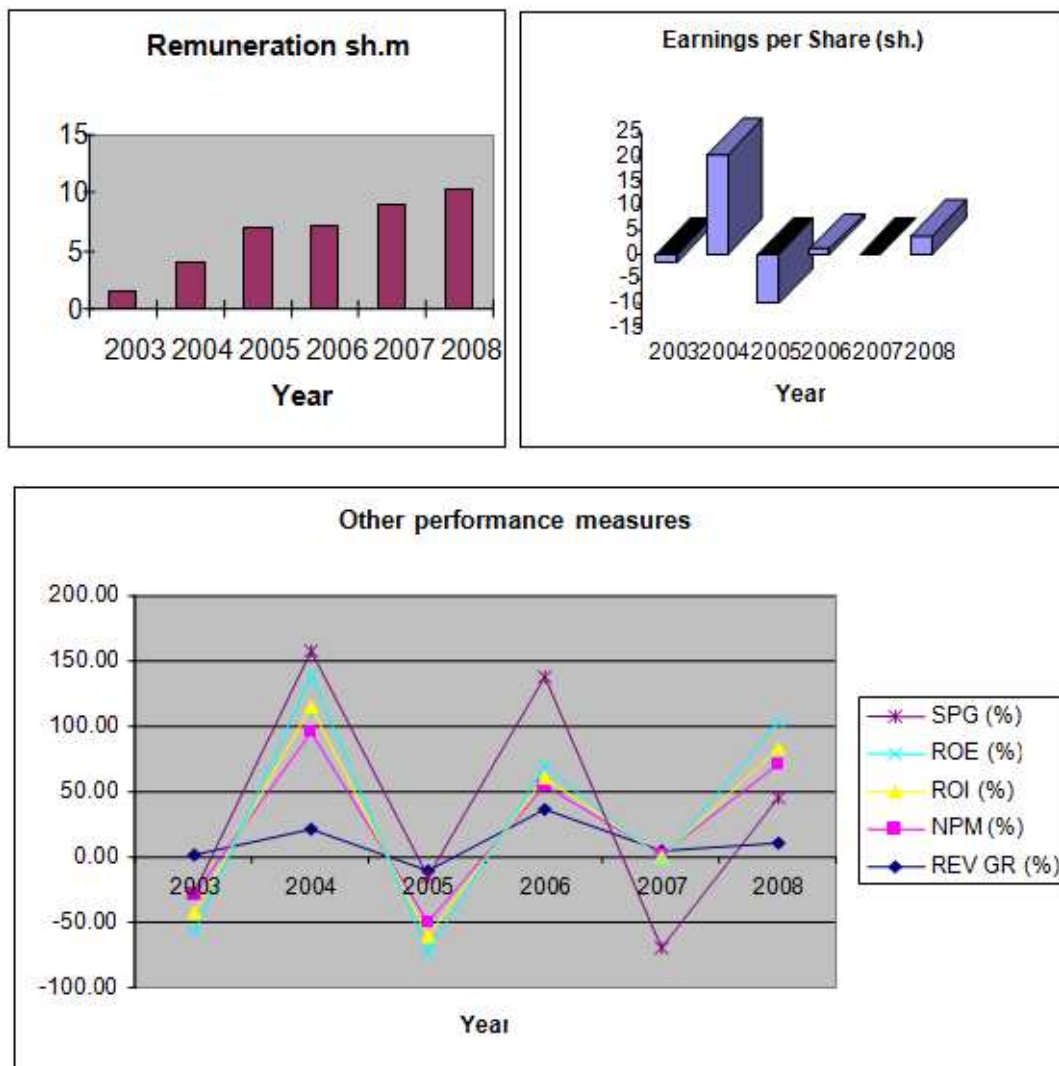
## Rea Vipingo



**Figure 3 - Rea Vipingo – Directors' remuneration & performance measures**

Remuneration has been increasing over the years with a higher amount reported in 2008. The earnings per share increased significantly in 2004 and have remained stable over the years. The share price growth was higher in 2005 but declined significantly in 2007. Most of the other performance measures had a general decline in 2005 but gained stability in 2006 and 2008. Even though the firm reported a general increase in production and sales of sisal, overall performance was affected by poor weather conditions and adverse changes in foreign currency. The stable performance was attributable to the volumes in sisal fibre and good performance of the Tanga Spinning Mill. The number of directors also remained the same throughout the period.

## Sasini



**Figure 4 - Sasini – Directors remuneration & performance measures**

A general increase in remuneration and Earnings per share with the highest remuneration paid in 2008 and highest Earnings Per share in 2004. Sasini reported a slightly volatility in performance in most of the other variables especially the Share Price Growth. The erratic performance was attributable to various factors such as low coffee production, poor economic conditions and declining global tea prices and adverse weather conditions. The good performance in 2006 was due to improving economy, but in 2007, there were adverse movements in foreign exchange rates and declining tea prices. The tea prices and coffee prices went up in 2008 despite the decline in coffee and tea production.

Table 1 provides the summary key statistics of the individual companies:

**Table 1 - Summary Remuneration & Firm Performance – Agricultural sector**

|             |     | REM  | REV     | NPM     | ROI    | ROE     | SPG     | EPS   |
|-------------|-----|------|---------|---------|--------|---------|---------|-------|
|             |     | Sh.m | GR%     | %       | %      | %       | %       | Sh.   |
| Kakuzi      | Max | 26.6 | 26.04%  | 17.47%  | 10.63% | 18.05%  | 173.04% | 13.12 |
|             | Min | 2.2  | -22.11% | -6.67%  | -3.59% | -8.13%  | -37.24% | -3.76 |
|             | Avg | 15.7 | 8.17%   | 6.33%   | 4.08%  | 7.49%   | 21.63%  | 4.92  |
| Rea Vipingo | Max | 31.6 | 26.46%  | 14.78%  | 12.54% | 22.40%  | 115.79% | 2.80  |
|             | Min | 10.8 | 4.40%   | 0.42%   | 0.34%  | 0.65%   | -23.33% | 0.05  |
|             | Avg | 19.2 | 12.86%  | 9.62%   | 9.25%  | 15.97%  | 48.76%  | 1.81  |
| Sasini      | Max | 10.2 | 36.16%  | 74.71%  | 19.33% | 24.23%  | 69.23%  | 20.29 |
|             | Min | 1.4  | -10.38% | -39.27% | -      | -15.01% | -68.18% | -     |
|             | Avg | 6.45 | 10.41%  | 13.60%  | 2.21%  | 3.56%   | 8.62%   | 2.18  |

The table also shows that Rea Vipingo paid the highest remuneration in the sector was also the best company terms of profitability.

Table 2 also summarises the average remuneration and performance for the sector over the six years:

**Table 2 - Annual remuneration and firm performance for agricultural sector**

|             | 2003  | 2004  | 2005  | 2006  | 2007  | 2008  | Average |
|-------------|-------|-------|-------|-------|-------|-------|---------|
| REM (sh. m) | 9.37  | 14.30 | 14.63 | 12.37 | 17.37 | 14.67 | 13.78   |
| REV GR (%)  | 10%   | 17%   | -2%   | 23%   | 6%    | 9%    | 10%     |
| NPM (%)     | -10%  | 32%   | -12%  | 13%   | 6%    | 30%   | 10%     |
| ROI (%)     | -4.6% | 12%   | -1%   | 8%    | 6%    | 11%   | 5%      |
| ROE (%)     | -5.1% | 18%   | 0.4%  | 12.6% | 10%   | 19%   | 9%      |
| SPG (%)     | 44%   | 92%   | 65%   | 27%   | -35%  | -35%  | 26%     |
| EPS (sh.)   | -0.77 | 8.90  | -3.95 | 3.24  | 3.82  | 6.59  | 2.97    |

The average remuneration has increased over the period but there is a general stability in the performance indicators except that of share price that has declined.

Table 3 summarises the regression results carried out for the individual companies over the six years:

**Table 3 - Individual company regression results - Agricultural sector**

|             | Remuneration Vs |         |         |         |         |           |
|-------------|-----------------|---------|---------|---------|---------|-----------|
|             | REV GR (%)      | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
| Kakuzi      | $\alpha$        | 16.46   | 19.38   | 19.51   | 18.95   | 13.8      |
|             | P( $\alpha$ )   | 0.016   | 0.006   | 0.007   | 0.009   | 0.004     |
|             | $\beta$         | -0.0929 | -0.5812 | -0.9327 | -0.4342 | 0.08591   |
|             | P( $\beta$ )    | 0.714   | 0.171   | 0.193   | 0.261   | 0.049     |
|             | R <sup>2</sup>  | 3.70%   | 41.00%  | 37.90%  | 29.90%  | 66.30%    |
|             | DW <sup>5</sup> | 1.03    | 1.8     | 2.01    | 1.6     | 1.53      |
| Rea Vipingo | $\alpha$        | 24.08   | 13.7    | 13.8    | 13.4    | 25.2      |
|             | P( $\alpha$ )   | 0.027   | 0.205   | 0.223   | 0.228   | 0.001     |
|             | $\beta$         | -0.3793 | 0.5675  | 0.5785  | 0.3609  | -0.1238   |
|             | P ( $\beta$ )   | 0.46    | 0.544   | 0.575   | 0.541   | 0.039     |
|             | R <sup>2</sup>  | 14.30%  | 9.90%   | 8.50%   | 10.00%  | 69.50%    |
|             | DW              | 1.05    | .811    | .751    | .79     | 1.96      |
| Sasini      | $\alpha$        | 6.38    | 6.23    | 6.28    | 6.28    | 6.71      |
|             | P( $\alpha$ )   | 0.024   | 0.015   | 0.012   | 0.013   | 0.006     |
|             | $\beta$         | 0.00615 | 0.01648 | 0.0772  | 0.06125 | -0.0302   |
|             | P( $\beta$ )    | 0.954   | 0.65    | 0.55    | 0.554   | 0.266     |
|             | R <sup>2</sup>  | 0.10%   | 5.70%   | 9.60%   | 9.40%   | 29.40%    |
|             | DW              | 0.419   | 0.611   | 0.749   | 0.743   | 0.810     |

The table shows mixed results but the main highlight is Kakuzi that is showing a negative relationship between executive remuneration and all but one of the performance indicators i.e share price growth. However the relations are not strong as given by the P values and R<sup>2</sup> (only that of share price is showing a significant positive relationship).

Rea Vipingo has reported a positive relationship between executive remuneration and firm performance for all the performance measures except for Revenue Growth and Share Price Growth. Again only that of share price growth shows a significant negative relationship. Sasini has also reported a positive relationship between executive remuneration and all the performance indicators except that of share price growth and Earnings Per Share. However none of the relationships as given by  $\beta$  are

<sup>5</sup> For individual companies where n=6 and k=1 the DW factors lie between 0.6 and 1.4 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

significant but the constants ( $\alpha$ ) are significant. A key conclusion from the table is that we fail to reject the null hypothesis i.e. there is no significant positive relationship between executive remuneration and firm performance.

Table 4 summarises the regression results for the entire Agricultural sector over the six years:

**Table 4 - Summary Regression – Agricultural sector**

| Remuneration Vs |               |         |         |            |            |              |
|-----------------|---------------|---------|---------|------------|------------|--------------|
|                 | REV<br>GR (%) | NPM (%) | ROI (%) | ROE<br>(%) | SPG<br>(%) | EPS<br>(sh.) |
| $\alpha$        | 14.5          | 13.95   | 12.8    | 12.4       | 13.3       | 14.407       |
| P( $\alpha$ )   | 0.00          | 0.00    | 0.00    | 0.00       | 0.00       | 0.00         |
| $\beta$         | -0.07         | -0.02   | 0.19    | 0.15       | 0.18       | -0.21        |
| P( $\beta$ )    | 0.673         | 0.845   | 0.452   | 0.37       | 0.606      | 0.528        |
| R <sup>2</sup>  | 1.1%          | 0.2%    | 3.6%    | 5%         | 1.7%       | 2.5%         |
| DW <sup>6</sup> | 1.5           | 1.9     | 1.7     | 1.8        | 2.1        | 2.101        |

As in the case of individual companies the performance indicators show a mixed relationship with executive remuneration but the P values show the relations are not significant. The constant factors appear to be more significant as given by the P value indicating that the main pay for the sector is the fixed pay. At this point we also fail to reject the Null hypothesis i.e. there is no significant positive relationship between executive remuneration and firm performance.

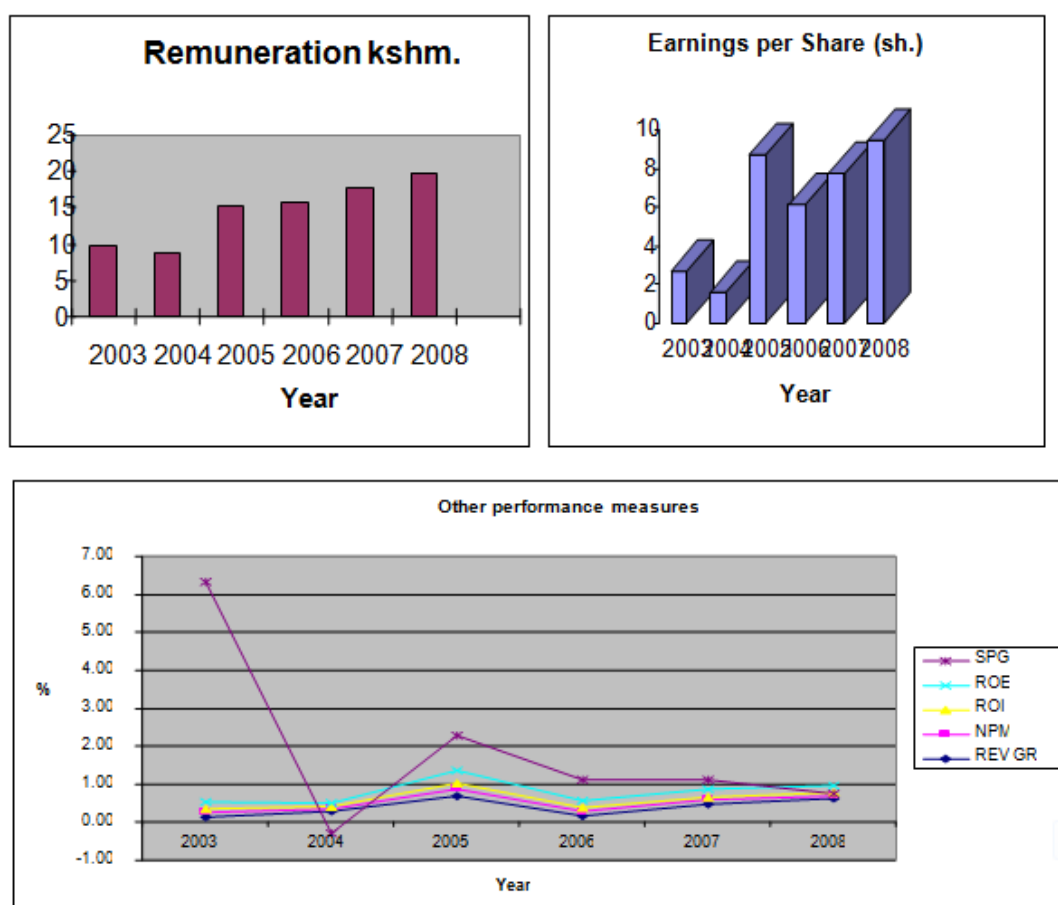
<sup>6</sup> For the sector analysis the where n=18 and k=1 the DW factors lie between 1.13 and 1.4 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

#### **4.2.2 Commercial and Services**

The companies in the commercial and service sector all reported a general increase in executive remuneration apart from Kenya Airways and Marshalls whose remuneration did not report a significant change. For the other performance measures, the earnings per share of most companies showed general increase except that of CMC Holdings and Marshalls. Other performance measures did not improve and just like for the agricultural sector, the share price growth was volatile.

Figures 5 to 11 summarise the trends in remuneration, the earnings per share and the other performance measures. The regression results also reported similar patterns as those of the Agricultural sector, some positive and some negative relations between executive remuneration and other performance measures but with no significance in the relationships. Tables 5 to 8 also present summary performance measures and regressions.

## Car and General

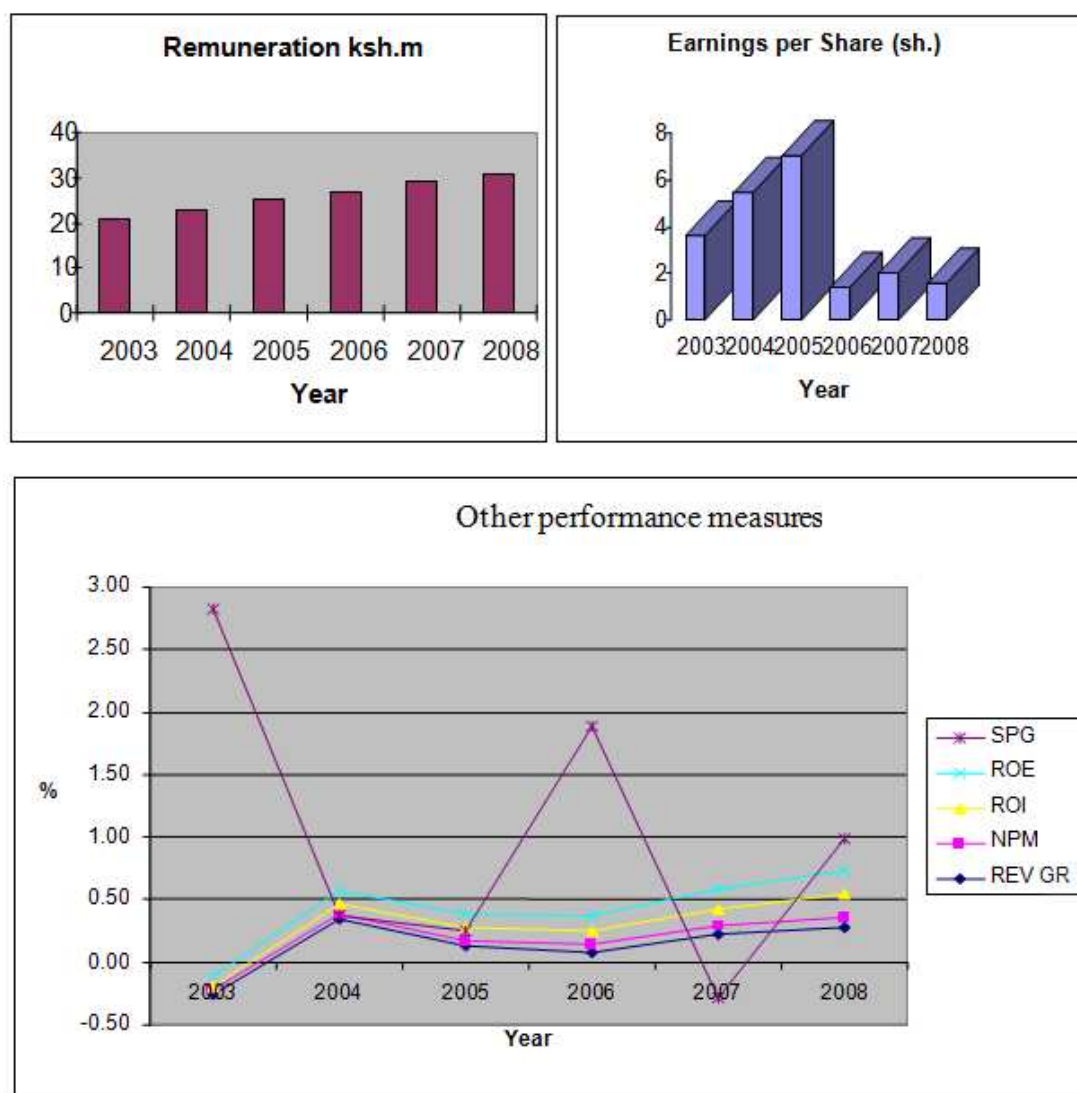


**Figure 5 - Car and General – Directors remuneration & performance measures**

Car and general reported an increase in the remuneration with the highest amount being that of 2008 and the lowest in 2004. The company reported lower Earnings Per Share in 2003 and 2004 but with a significant increase in 2005. This has been stable up to 2008. The company also reported a stable performance for most of the other performance measures apart from Share Price Growth which was high in 2003 but declined significantly in 2004.

As in 2005, the decline in performance in 2004 was attributable to adverse foreign exchange rates and high competition especially from China. But with expansion in the region and good sales of the generator business the company was able to improve its overall performance until 2008 when performance declined due to the post election violence. However the decline is not significant because other regional operations like in Uganda and Ethiopia reported good results. The company also saw a growth in various brands.

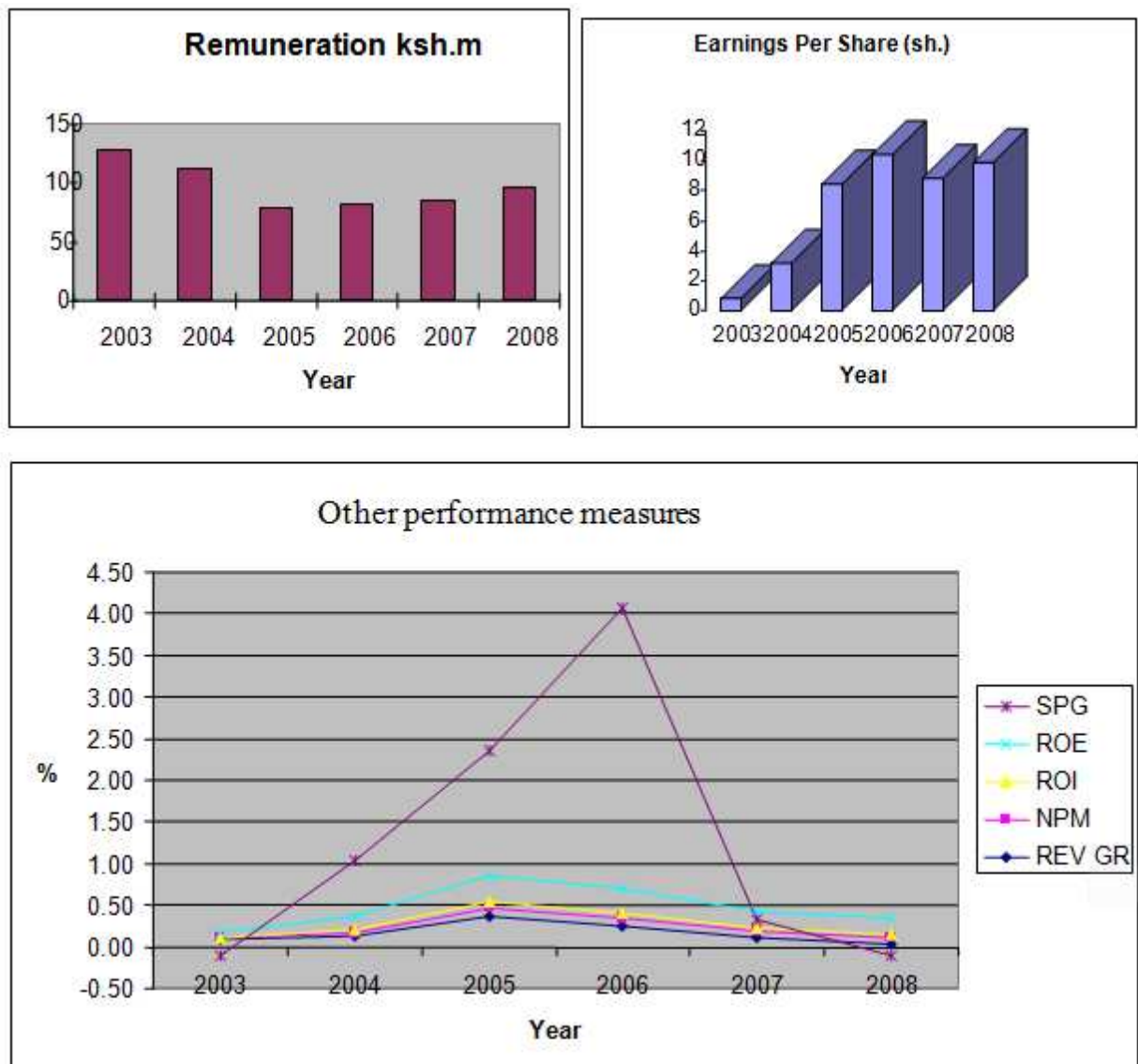
## CMC Holdings



**Figure 6 - CMC Holdings – Directors remuneration & performance measures**

For CMC holdings, there was a general increase in executive remuneration over the years but not very significant with the highest amount reported in 2008. This is despite the fact that the number of directors still remained the same (about 7). There was an initial increase in Earnings per Share from 2003 to 2005 but a significant decline in 2006. This has remained at the same level from 2006 to 2008. CMC holdings had a general improvement in other measures apart from Share price growth which reported significant volatility over time. The company's general improvement in performance was attributable mainly to high sales of commercial vehicles and spare parts and introduction of various brands.

## Kenya Airways

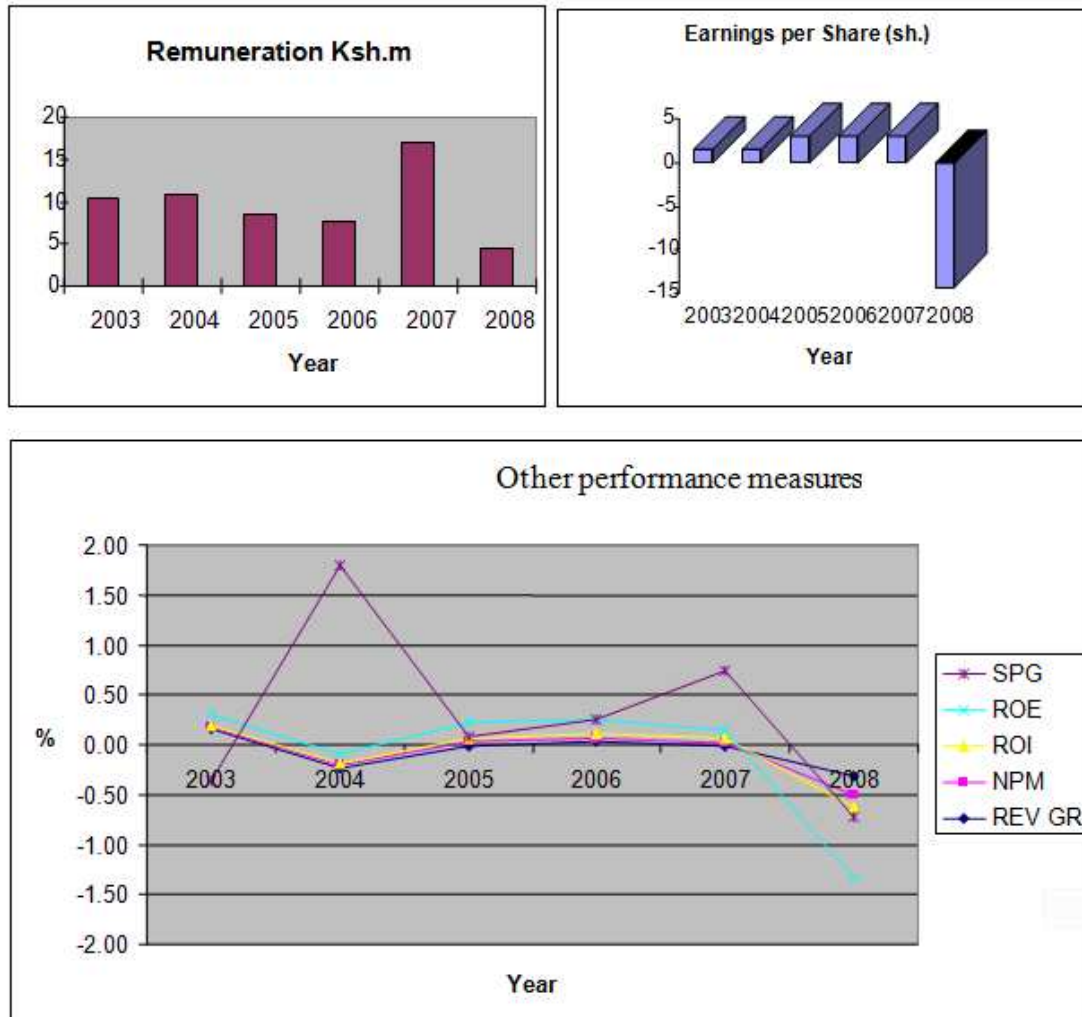


**Figure 7 - Kenya Airways – Directors remuneration & performance measures**

For Kenya airways there was a general stability in remuneration but with a downward trend. No explanation is given for this but like most of the companies, the number of directors remained the same. The highest amount paid was in 2003. This shows a significant improvement in Earnings Per Share in 2005 but with some stability until 2008. The Share Price Growth had a significant improvement between 2003 and 2006, but again a significant decline in 2007 and 2008. There was general stability in the other performance measures. The initial increase level of performance was due to increase in the passenger traffic and a boost in the cargo business. Even though the performance declined marginally from 2005, this was mitigated by proper cost

management and hedging strategies. The decline in performance was due to adverse changes in the foreign exchange market coupled with stiff competition in various routes.

## Marshall's

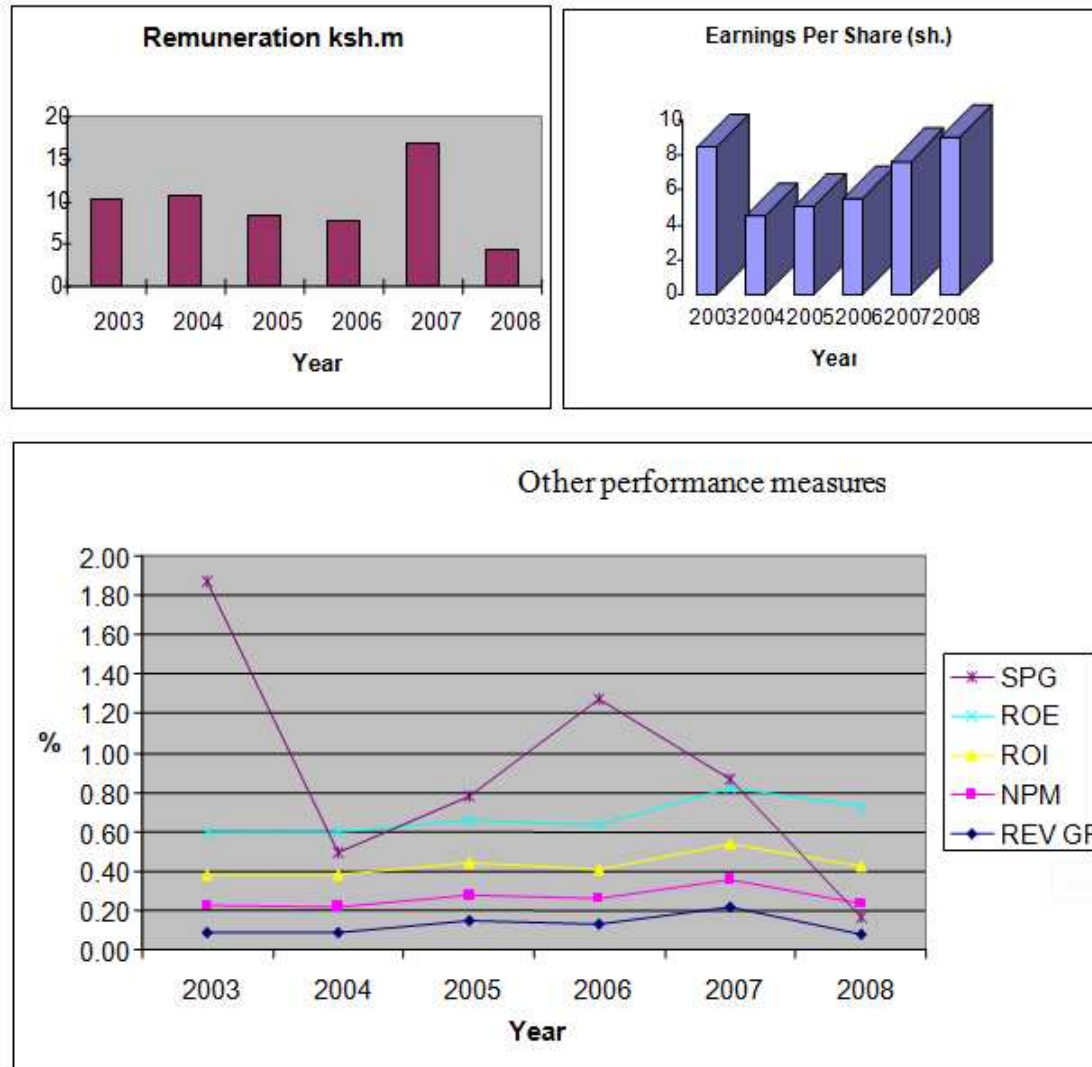


**Figure 8 - Marshall's East Africa – Directors remuneration & performance measures**

The trend shows a significant variation in remuneration but a general downward trend with the highest amount reported in 2007 and the lowest in 2008. Again no reason is provided for and the number of directors remained the same (7). The performance shows stable Earnings Per Share between 2003 and 2007, but a significant decline in 2008. All the performance measures reported a general decrease with the share price growth still being volatile. The initial good performance was attributable to growth in commercial vehicle sales and good margins, favourable exchange rates and in 2006,

the company invested in Tata holdings in order to boost its export sales. But in 2008, the firm was affected by the negative impact of post election violence.

## Nation Media

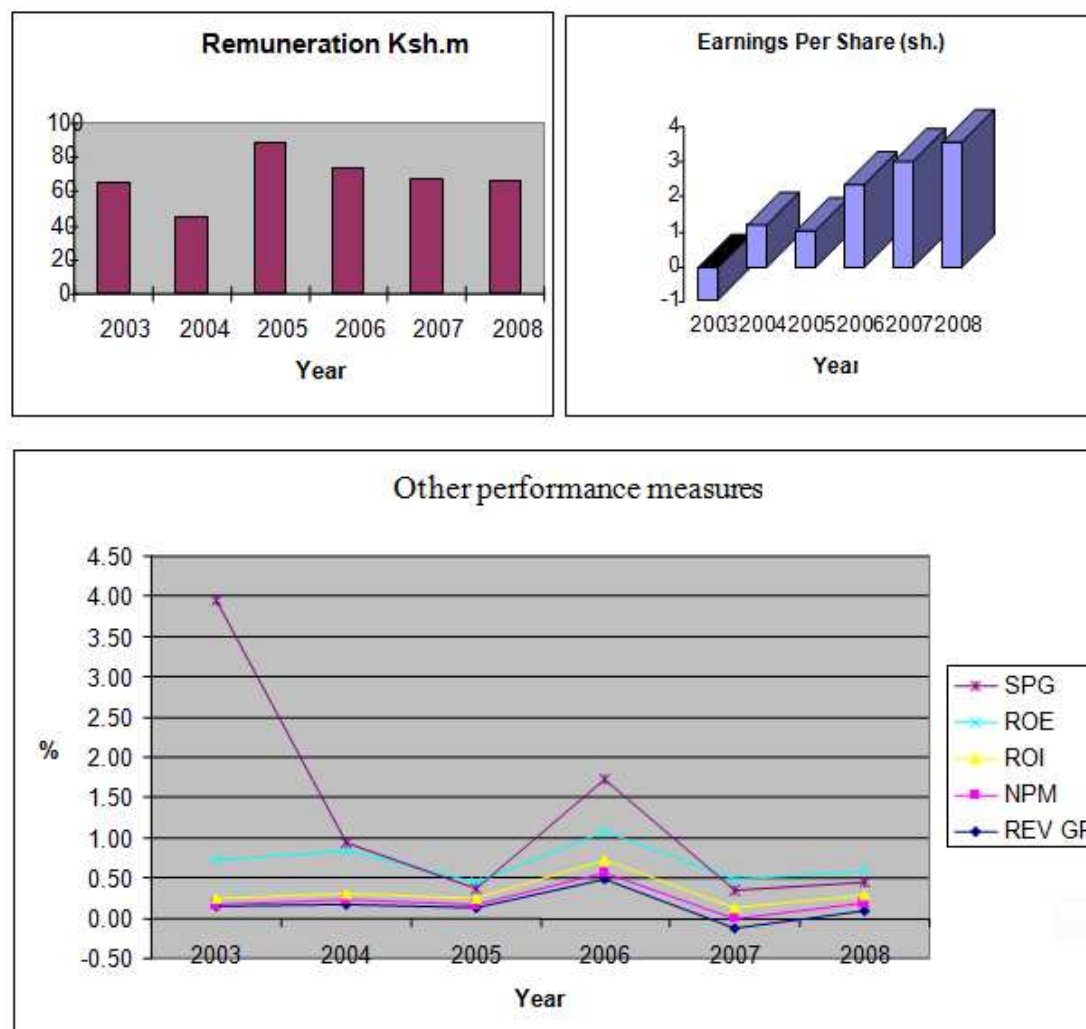


**Figure 9 - Nation Media Group – Directors remuneration & performance measures**

Executive remuneration was generally stable, but with a declining trend with the number of directors remaining stable (12). The highest amount was paid in 2007 and the lowest in 2008. For performance measures, The Earnings Per Share has had a general increase from 2004 to 2008. However this was coming from a significant decline from 2003. Most of the performance measures remained stable over time except for the share price growth which shows some volatility. The relative good performance was largely attributable to sale of newspapers and rapid expansion

within the local and foreign markets in order to consolidate its position in the region as a leading media company.

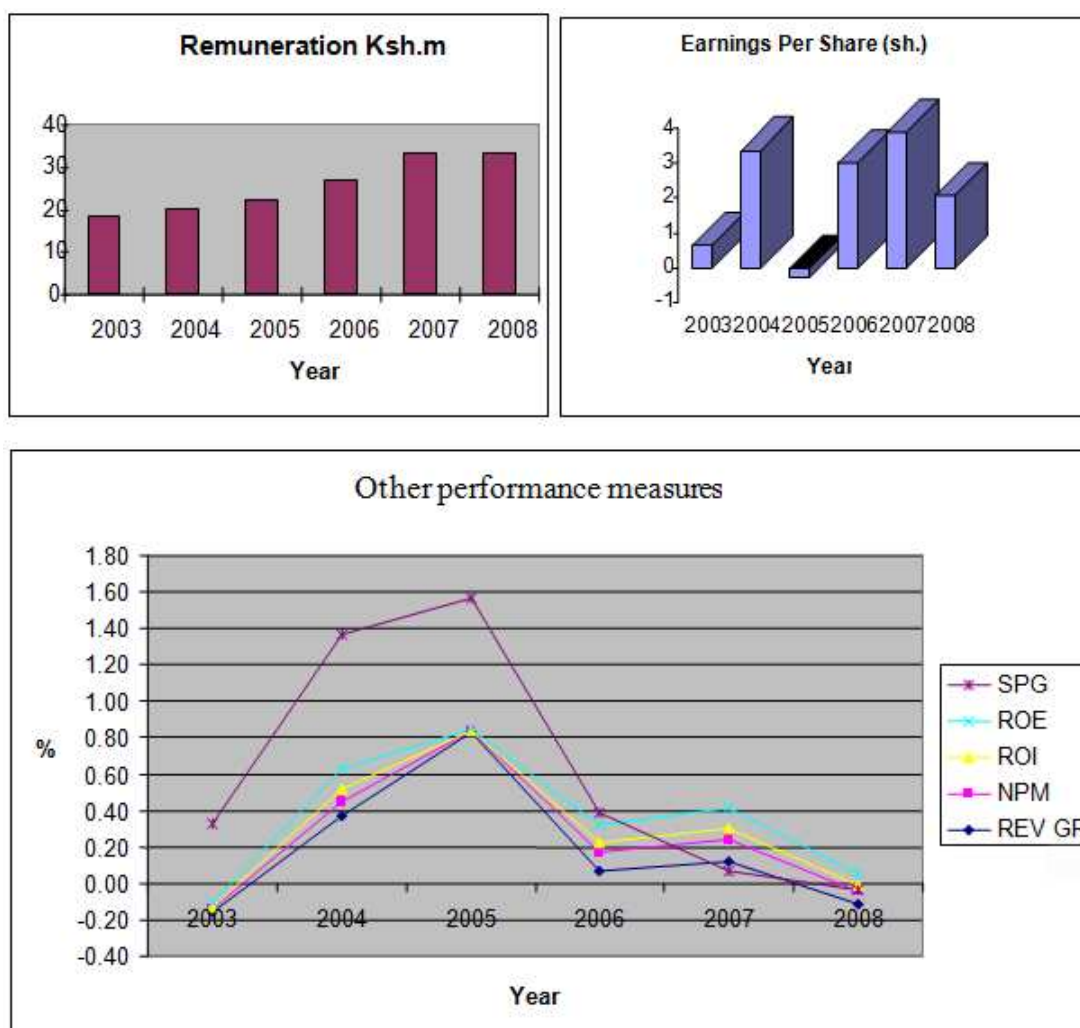
### Standard Group



**Figure 10 - Standard Group – Directors remuneration & performance measures**

The executive remuneration has been stable except for the year 2005 when it was slightly higher. The number of directors also remained the same over the same period. There was a general improvement in the Earnings per Share from a negative in 2003 to the highest peak in 2008. The performance measures show a relative stability except for the share price growth which has a significant decline. The main reason for the stability in performance was due to increased advertising and viewership and control of costs. The company also carried out major restructuring as well as staff rationalization.

## TPS Serena



**Figure 11 - TPS Serena – Directors remuneration & performance measures**

TPS Serena had a general increase in remuneration which stabilised in 2007 and 2008. The number of directors increased from 8 to 13 as a result of reorganization. The Earnings per Share has shown a general stability except in 2005 when it declined significantly. The other performance measures increased significantly from 2003 to 2005 when the trend reversed to a general decline. The improved performance in 2003 to 2005 was due to improved tourism in the country and moving into new markets. The decline thereafter was due to operational costs, poor infrastructure and, the group was affected by post election violence in 2008. This was mitigated by trying to cut down costs but maintaining the quality of services.

Table 5 provides highlights of the key performance for each company in the sector:

**Table 5 - Summary Remuneration and Firm Performance – Commercial & Services**

|                |     | REM   | REV     | NPM    | ROI     | ROE     | SPG     | EPS   |
|----------------|-----|-------|---------|--------|---------|---------|---------|-------|
|                |     | Sh.m  | GR%     | %      | %       | %       | %       | Sh.   |
| Car & General  | Max | 19.7  | 68.84%  | 18.27% | 16.72%  | 32.17%  | 580.00% | 9.50  |
|                | Min | 8.7   | 11.90%  | 5.88%  | 4.99%   | 9.30%   | -77.94% | 1.64  |
|                | Avg | 14.4  | 39.54%  | 10.69% | 9.74%   | 19.33%  | 109.39% | 6.06  |
| CMC Holdings   | Max | 30.6  | 34.61%  | 8.07%  | 18.27%  | 19.17%  | 294.20% | 7.00  |
|                | Min | 20.5  | -25.71% | 3.85%  | 2.60%   | 7.52%   | -87.10% | 1.43  |
|                | Avg | 25.8  | 13.24%  | 5.67%  | 10.73%  | 12.50%  | 58.53%  | 3.52  |
| Kenya Airways  | Max | 129   | 36.31%  | 9.19%  | 8.66%   | 31.46%  | 337.50% | 10.45 |
|                | Min | 79    | 2.59%   | 1.32%  | 1.49%   | 4.93%   | -44.74% | 0.75  |
|                | Avg | 97.17 | 16.23%  | 6.40%  | 5.44%   | 19.49%  | 78.91%  | 6.92  |
| Marshall's     | Max | 17    | 15.93%  | 3.45%  | 4.35%   | 14.93%  | 189.26% | 3.11  |
|                | Min | 4.3   | -30.73% | -      | -14.05% | -70.54% | -66.94% | -     |
|                | Avg | 9.7   | -6.03%  | 18.99% | 0.39%   | -2.07%  | 38.42%  | 14.24 |
| Nation Media   | Max | 109.1 | 21.25%  | -0.97% | 19.58%  | 30.03%  | 127.38% | -0.36 |
|                | Min | 37.5  | 7.36%   | 15.71% | 14.80%  | 21.76%  | -56.44% | 9.03  |
|                | Avg | 69.58 | 12.45%  | 13.59% | 16.65%  | 24.49%  | 23.43%  | 4.50  |
| Standard Group | Max | 89    | 49.14%  | 11.12% | 15.88%  | 52.54%  | 322.87% | 6.69  |
|                | Min | 45    | -12.04% | 3.18%  | 6.72%   | 20.11%  | -14.29% | 3.57  |
|                | Avg | 67.72 | 14.82%  | 6.72%  | 10.56%  | 37.00%  | 60.43%  | -0.95 |
| TPS Serena     | Max | 33.3  | 82.95%  | 11.34% | 6.33%   | 11.90%  | 73.39%  | 1.70  |
|                | Min | 18.4  | -16.07% | 0.75%  | 0.46%   | 0.96%   | -34.10% | 3.91  |
|                | Avg | 25.65 | 18.63%  | 6.50%  | 3.84%   | 7.07%   | 25.51%  | -0.28 |
|                |     |       |         |        |         |         |         | 2.13  |

Table 5 shows that Kenya Airways paid the highest remuneration to its directors followed by Nation Media. Marshall's paid the lowest amounts. All the companies performed well with Car and General reporting the best revenue growth and shareholders return.

Table 6 summarises the average revenue and performance for the sector over the six years:

**Table 6 - Annual remuneration and firm performance - Commercial and services sector**

|             | 2003    | 2004   | 2005   | 2006   | 2007   | 2008   | Average |
|-------------|---------|--------|--------|--------|--------|--------|---------|
| REM (sh. m) | 42.54   | 36.69  | 43.73  | 45.86  | 51.29  | 45.63  | 44.29   |
| REV GR (%)  | 2.61%   | 16.60% | 32.51% | 17.54% | 14.63% | 9.43%  | 16%     |
| NPM (%)     | 5.36%   | 6.05%  | 7.58%  | 8.44%  | 9.00%  | 5.22%  | 7%      |
| ROI (%)     | 5.76%   | 7.38%  | 9.11%  | 9.69%  | 9.87%  | 7.35%  | 8%      |
| ROE (%)     | 16.07%  | 18.67% | 18.94% | 20.12% | 19.95% | 7.22%  | 17%     |
| SPG (%)     | 182.03% | 33.00% | 41.53% | 97.45% | -7.84% | -7.91% | 56%     |
| EPS (sh.)   | 2.40    | 2.97   | 4.69   | 4.56   | 5.16   | 3.07   | 3.81    |

The average remuneration for the sector has been increasing but it reduced sharply in 2008. Performance improved between 2005 and 2006 and started to decline sharply in 2008.

Table 7 summarizes the regression results for the individual companies:

**Table 7 - Companies regression results- Commercial & Services**

|                           | Remuneration Vs |               |            |            |            |            |              |
|---------------------------|-----------------|---------------|------------|------------|------------|------------|--------------|
|                           |                 | REV GR<br>(%) | NPM<br>(%) | ROI<br>(%) | ROE<br>(%) | SPG<br>(%) | EPS<br>(sh.) |
| Car & General<br>Kenya    | $\alpha$        | 9.7           | 14         | 12.6       | 8.84       | 15.3       | 6.66         |
|                           | P( $\alpha$ )   | 0.03          | 0.069      | 0.091      | 0.17       | 0.002      | 0.11         |
|                           | $\beta$         | 0.11876       | 0.0413     | 0.1827     | 0.2876     | -0.0078    | 1.2766       |
|                           | P( $\beta$ )    | 0.164         | 0.938      | 0.756      | 0.329      | 0.398      | 0.005        |
|                           | R <sup>2</sup>  | 41.90%        | 0.20%      | 2.70%      | 23.50%     | 18.20%     | 89.20%       |
|                           | DW              | 1.07          | 0.8        | 0.45       | 0.9        | 1.33       | 1.8          |
| CMC Holdings              | $\alpha$        | 24.4          | 12.6       | 18.3       | 14.8       | 26.7       | 29.1         |
|                           | P( $\alpha$ )   | 0.00          | 0.00       | 0.00       | 0.001      | 0.00       | 0.00         |
|                           | $\beta$         | 0.10372       | 2.3206     | 0.6959     | 0.8834     | -0.0157    | -0.932       |
|                           | P( $\beta$ )    | 0.223         | 0.001      | 0.001      | 0.001      | 0.228      | 0.247        |
|                           | R <sup>2</sup>  | 34.20%        | 95.80%     | 95.80%     | 93.90%     | 33.50%     | 31.40%       |
|                           | DW              | 0.9           | 1.39       | 2          | 1.1        | 0.86       | 1.1          |
| Kenya Airways             | $\alpha$        | 112.1         | 136.8      | 138.1      | 134.8      | 102.7      | 128.5        |
|                           | P( $\alpha$ )   | 0.001         | 0.000      | 0.000      | 0.000      | 0.000      | 0.000        |
|                           | $\beta$         | -0.9229       | -6.1961    | -7.52      | -1.9312    | -0.0705    | -4.5286      |
|                           | P( $\beta$ )    | 0.231         | 0.001      | 0.007      | 0.007      | 0.285      | 0.009        |
|                           | R <sup>2</sup>  | 33.30%        | 95.20%     | 86.60%     | 86.50%     | 27.50%     | 85.10%       |
|                           | DW              | 0.34          | 2.1        | 1.37       | 1.02       | 1.12       | 1.64         |
| Marshall's East<br>Africa | $\alpha$        | 10.3          | 9.9        | 9.56       | 9.85       | 9.44       | 9.83         |
|                           | P( $\alpha$ )   | 0.006         | 0.003      | 0.004      | 0.003      | 0.011      | 0.003        |
|                           | $\beta$         | 0.092         | 0.2965     | 0.3505     | 0.07328    | 0.00689    | 0.3856       |
|                           | P( $\beta$ )    | 0.461         | 0.189      | 0.219      | 0.227      | 0.786      | 0.188        |
|                           | R <sup>2</sup>  | 14.20%        | 38.40%     | 34.60%     | 33.70%     | 2.10%      | 38.60%       |
|                           | DW              | 2             | 1.8        | 2.1        | 2.1        | 2.105      | 1.95         |
| Nation Media Group        | $\alpha$        | 18.7          | 46.8       | 17.7       | 23.9       | 71.2       | 52.5         |
|                           | P( $\alpha$ )   | 0.414         | 0.775      | 0.881      | 0.755      | 0.005      | 0.328        |
|                           | $\beta$         | 4.087         | 1.69       | 5.248      | 3.822      | -0.0706    | 2.554        |
|                           | P( $\beta$ )    | 0.057         | 0.887      | 0.475      | 0.258      | 0.748      | 0.727        |
|                           | R <sup>2</sup>  | 63.80%        | 0.60%      | 13.40%     | 30.30%     | 2.90%      | 3.40%        |
|                           | DW              | 1.04          | 0.99       | 1.2        | 1.33       | 1.16       | 0.94         |
| Standard Group            | $\alpha$        | 66.5          | 71.28      | 67.9       | 105.03     | 68.2       | 67.13        |
|                           | P( $\alpha$ )   | 0.001         | 0.011      | 0.040      | 0.001      | 0.001      | 0.002        |
|                           | $\beta$         | 0.0811        | -0.534     | -0.022     | -1.0247    | -0.0093    | 0.343        |
|                           | P( $\beta$ )    | 0.832         | 0.815      | 0.992      | 0.028      | 0.871      | 0.941        |
|                           | R <sup>2</sup>  | 1.30%         | 1.50%      | 0.00%      | 74.10%     | 0.70%      | 0.20%        |
|                           | DW              | 2.102         | 2.101      | 2          | 1.7        | 1.98       | 2.1          |
| TPS Serena                | $\alpha$        | 26.65         | 19.38      | 21.78      | 22.1       | 29         | 21.48        |
|                           | P( $\alpha$ )   | 0.001         | 0.012      | 0.015      | 0.015      | 0.000      | 0.009        |
|                           | $\beta$         | -0.05374      | 0.9638     | 1.008      | 0.4983     | -0.1317    | 1.957        |
|                           | P( $\beta$ )    | 0.559         | 0.178      | 0.442      | 0.49       | 0.017      | 0.321        |

|                |       |        |        |        |        |        |
|----------------|-------|--------|--------|--------|--------|--------|
| R <sup>2</sup> | 9.20% | 40.00% | 15.40% | 12.60% | 79.30% | 24.20% |
| DW             | 0.48  | 1.29   | 0.066  | 0.58   | 1.49   | 0.8    |

The major highlight of the regression results is that Kenya Airways is the only company to show a significant negative relationship between executive remuneration and firm performance (only share price growth is not significant). Marshalls East Africa reported a positive relationship in all the performance indicators but none of the relations are significant. Car and General and Nation Media reported a positive relationship with all the performance indicators except for Share Price Growth where all the relations were not significant. The other companies have reported varied relationships which are not significant. Again, apart from the results of CMC Holdings and Kenya Airways we fail to reject the null hypothesis and conclude that there is no evidence of a strong positive relationship between executive remuneration and firm performance for the other companies.

Table 8 gives the summary regression results for the entire Commercial and Services:

**Table 8 - Summary Regression – Commercial and Services**

| Remuneration Vs |            |         |         |         |         |           |
|-----------------|------------|---------|---------|---------|---------|-----------|
|                 | REV GR (%) | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
| $\alpha$        | 44.21      | 35.1    | 32.4    | 32.4    | 45.5    | 35.6      |
| P( $\alpha$ )   | 0.00       | 0.00    | 0.00    | 0.00    | 0.00    | 0.00      |
| $\beta$         | 0.004      | 1.3     | 1.44    | 0.704   | -0.02   | 2.2       |
| P( $\beta$ )    | 0.984      | 0.146   | 0.084   | 0.016   | 0.614   | 0.07      |
| R <sup>2</sup>  | 0%         | 5.2%    | 7.3%    | 13.6%   | 0.6%    | 0.8%      |
| DW <sup>7</sup> | 2          | 1.9     | 1.85    | 2.1     | 2.1     | 2.101     |

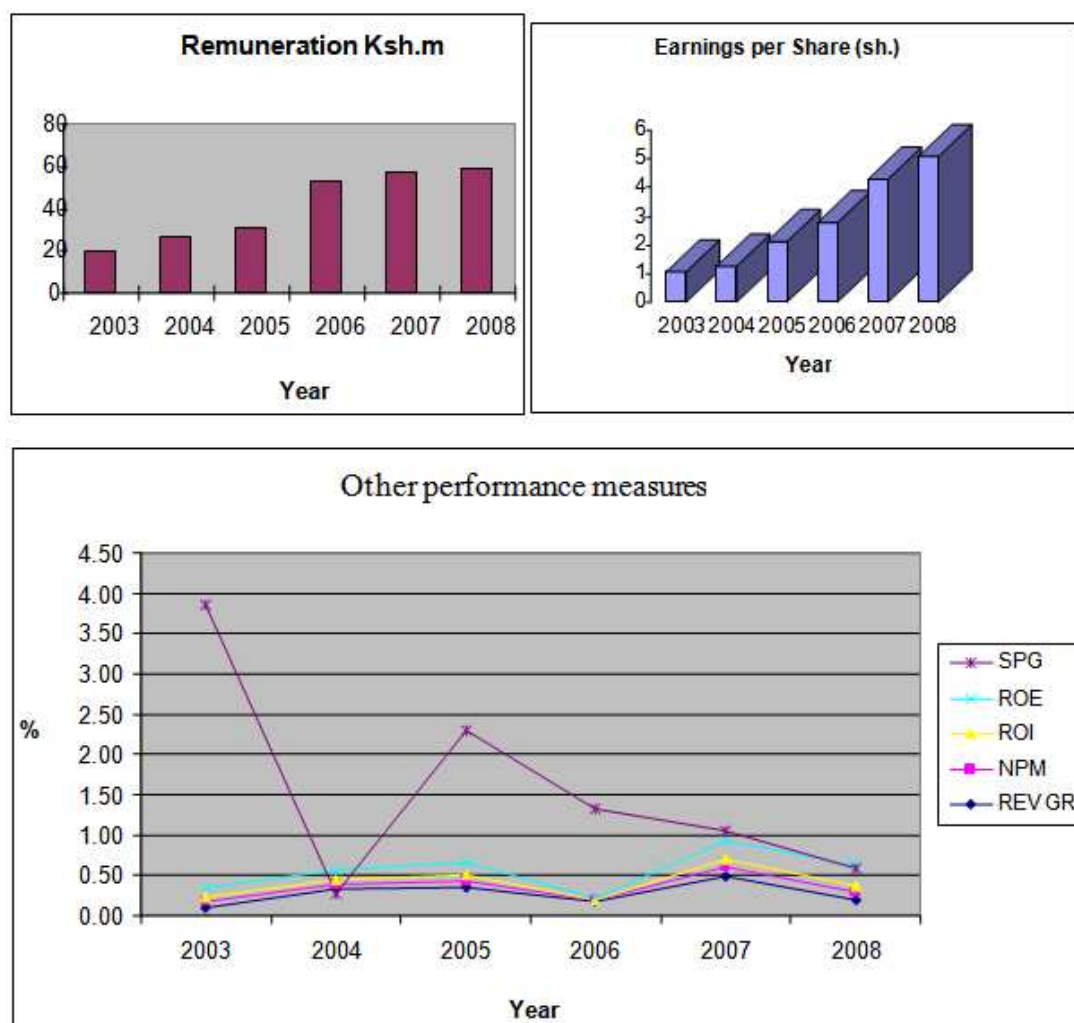
Majority of the performance indicators show a positive relationship with executive remuneration, except that of share price growth. The beta indicates that the relationships are not significant while the alphas (being the fixed pay) are significant. Again for the entire sector, we fail to reject the null hypothesis as conclude that there is no evidence of a strong positive relationship between executive remuneration and firm performance.

<sup>7</sup> For the sector analysis the where n=42 and k=1 the DW factors lie between 1.4 and 1.6 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

### **4.2.3 Industrial and Allied**

Generally, there has been an increase in executive remuneration for all the companies over the years except for Marshalls and Unga group. The earnings Per Share has also increased over time, but the other performance measures have not improved just like in the other sectors. The share prices of the companies have been volatile with significant declines and increases. Figure 12 to 25 provide trends to analyse the companies. The regression analysis carried out on remuneration and other factors also did not find any significant relationships. Tables 9 to 12 provide important information on the executive remuneration and firm performance and in addition, a summary of regression results.

## Athi River



**Figure 12 - Athi River Mining Company – Directors remuneration & performance measures**

There is a general increase in the remuneration with higher levels reported in 2007 and 2008. The number of directors remained the same over the six years. A similar trend is also observed for Earnings per Share, consistently increasing from one period to the next with higher levels in 2008. The company reported a general decline in the share price growth but a modest increase in the other performance indicators.

The good performance of the company is largely attributable to increased demand in cement, major investments to boost capacity, and improvement in exports. The company has also consolidated its position in the region and diversified its product base.

## Bamburi Cement

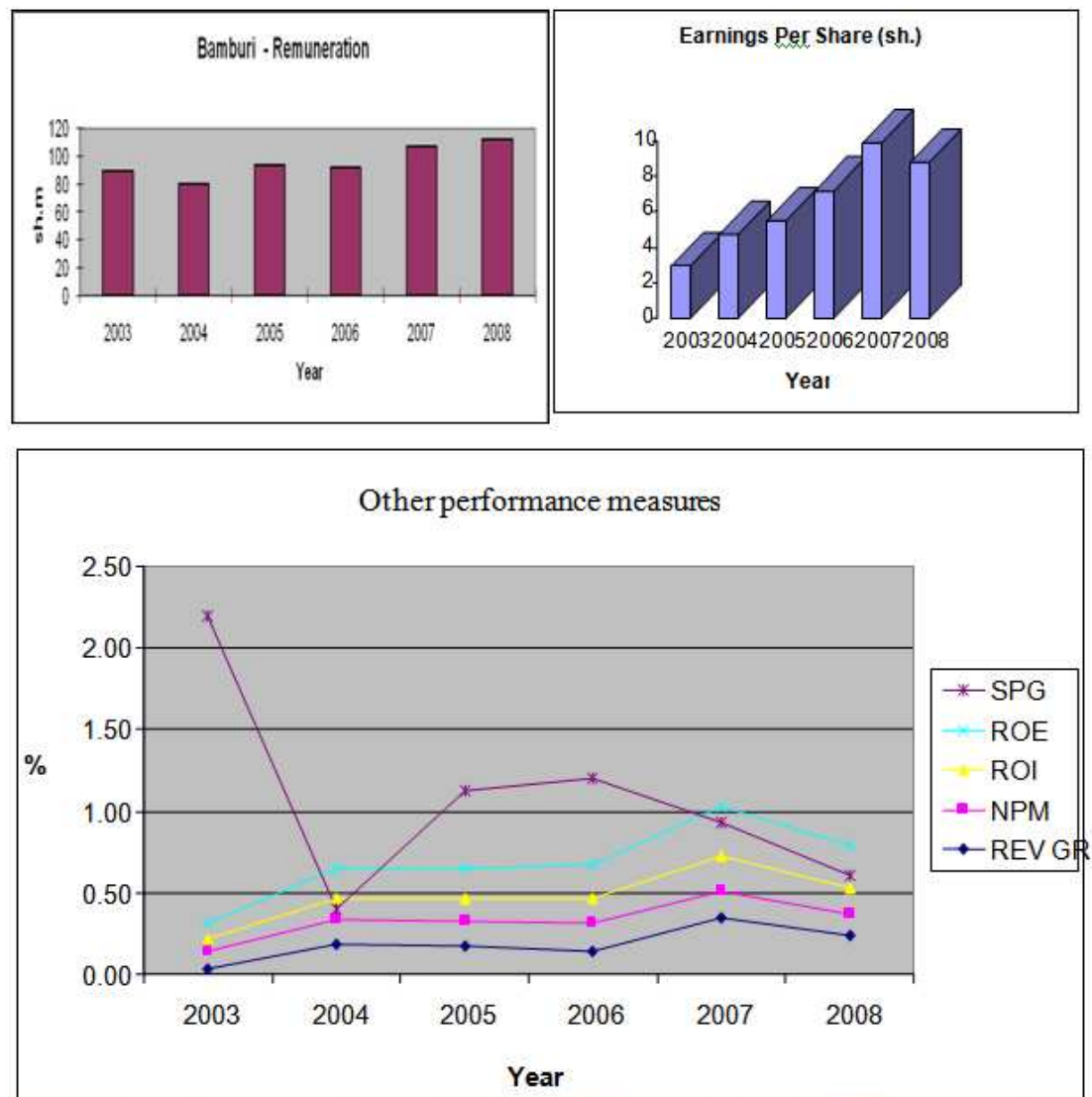
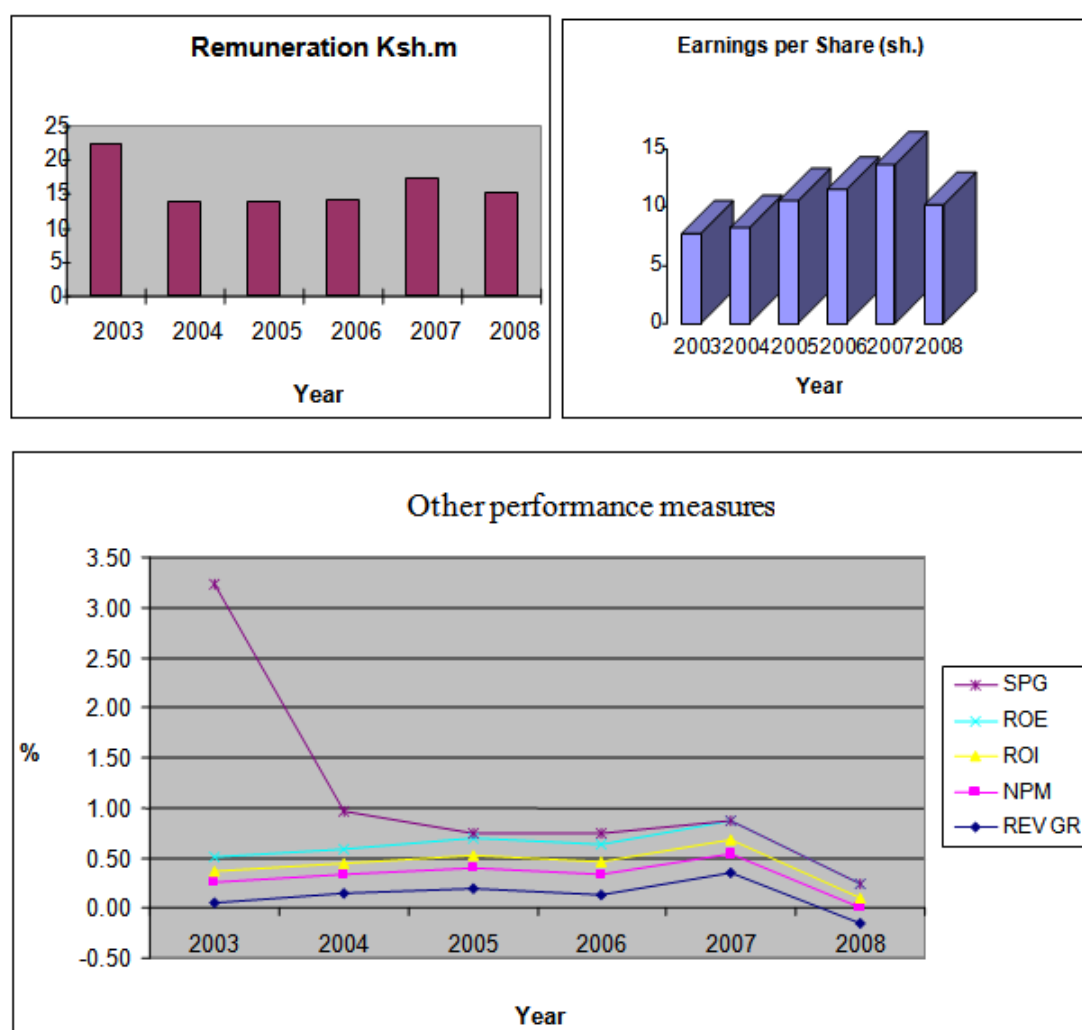


Figure 13 - Bamburi Cement – Directors remuneration & performance measures

As like in the case of Athi River Mining, Bamburi Cement reported a general increase in remuneration with a higher amount paid in 2008. The company also reported a general increase in Earnings per Share but the trend reversed in 2008 when there was a slight decrease. There is a general increase in most of the performance measures except for the Share Price growth. The company attributed its performance to increased demand in cement and other operational efficiencies.

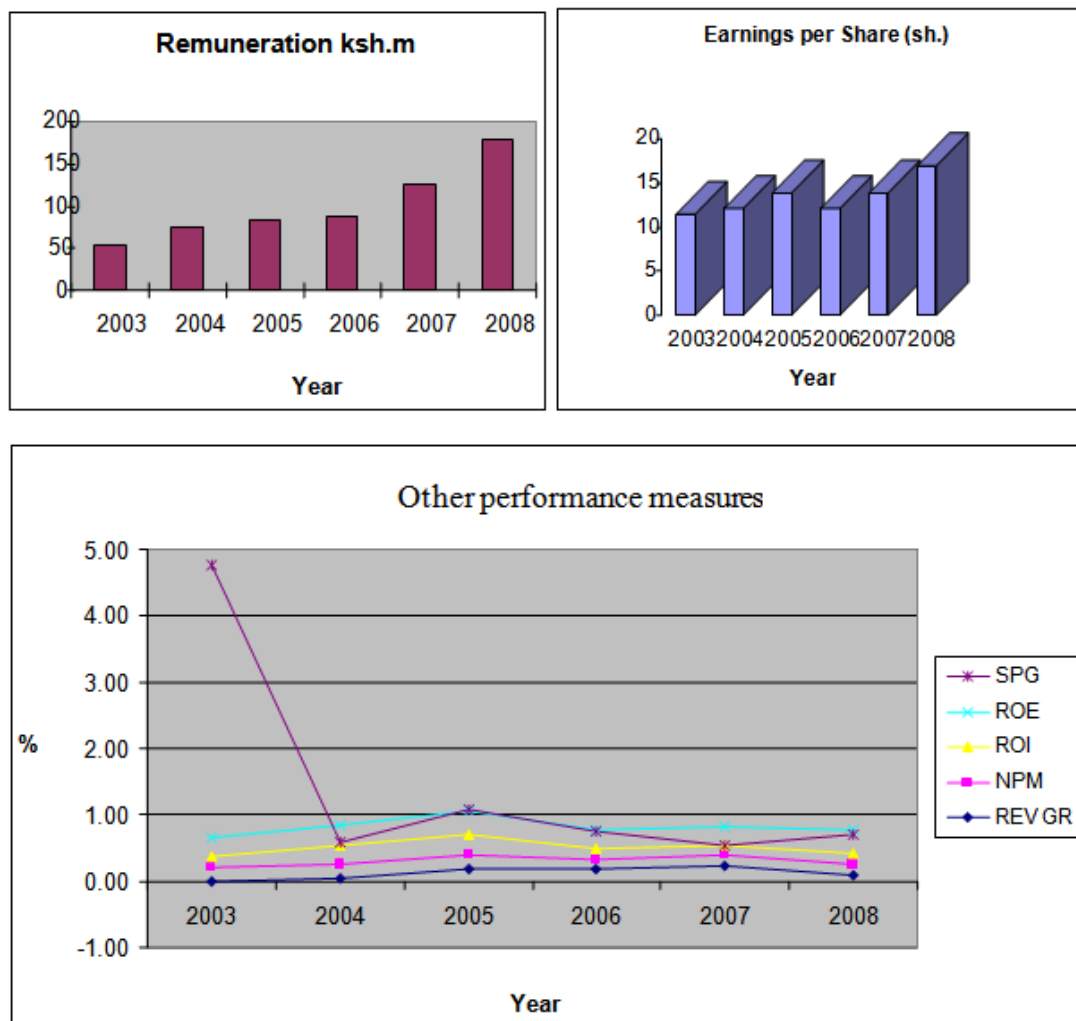
## Boc Gases



**Figure 14 - BOC Gases – Directors remuneration & performance measures**

BOC Gases reported a general stability in the remuneration and also the number of directors, but the highest amount was that paid in 2003. The Earnings per Share has been increasing except for 2008 when it declined. The Share Price Growth has been declining but the other performance measures have remained stable until 2008 when there was a modest decline. The initial good performance was due to increase in sales of gas products, focus on cost reduction and expansion. The company also embarked on an aggressive marketing strategy. The decline in performance in 2008 was largely attributable to the negative effects of the post election violence.

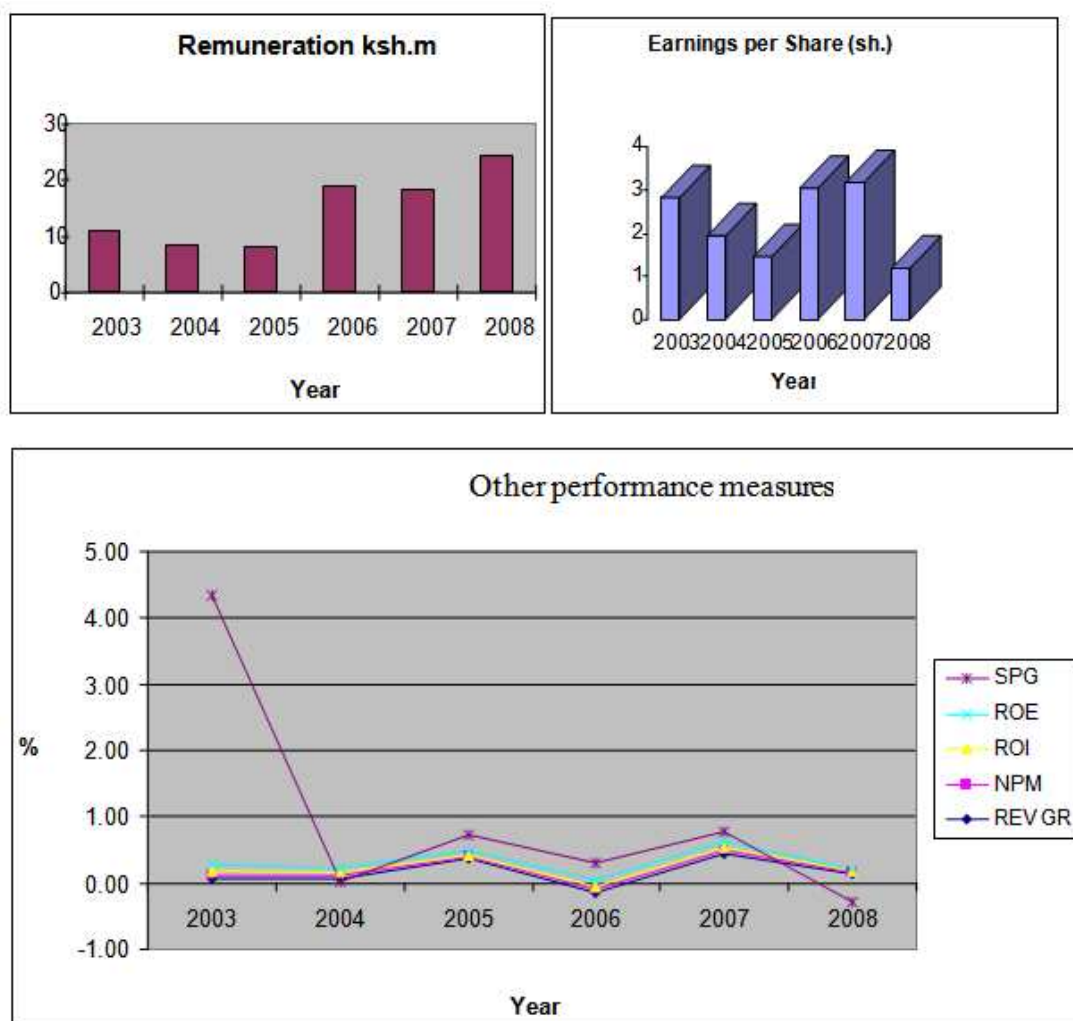
## British American Tobacco



**Figure 15 - British American Tobacco – Directors remuneration & performance measures**

A consistent increase in remuneration over the years with the highest amount reported in 2008 and the number of directors remaining the same (about 10). The Earnings per Share has also increased over time but not significantly. Just like the other companies in the sector, the share price has been declining over time except in 2005 when there was a slight increase. However, the other performance measures remained stable with no improvement or decline. The company reported increased export sales, and due to adverse legal environment, the company focused on cost management strategies, product mix and enhancing some of its brands. The government introduced the Tobacco Control Act which limits its ability to market its products aggressively and is also subject to stiff competition and high taxes.

## Crown Berger

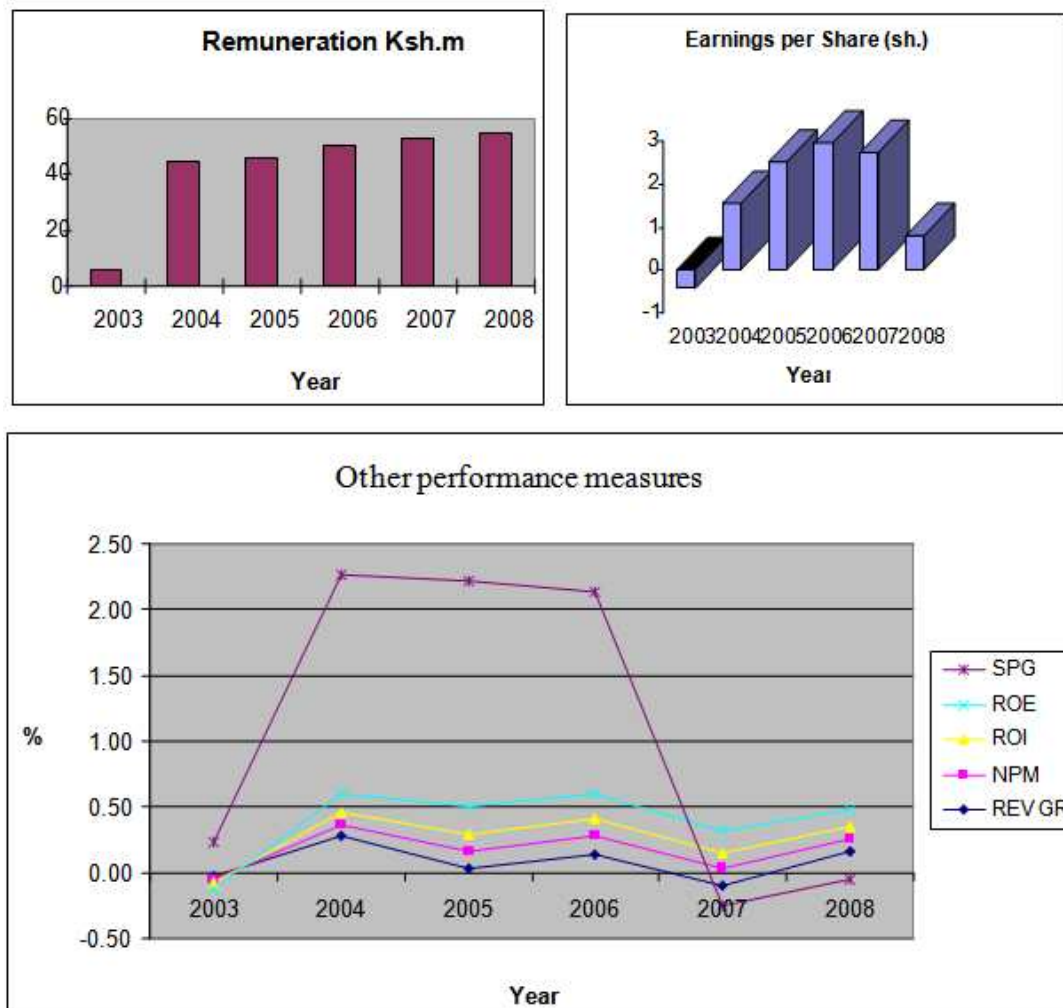


**Figure 16 - Crown Berger- Director's remuneration & performance measures**

The firm reported a general increase in directors' remuneration with the number of directors remaining the same. There was a slight decrease from 2003 to 2005 and significant increase from 2006 with the highest level in 2008. The Earnings per Share had a mixed trend with a general decrease from 2003 to 2004, but a significant increase in 2006. There was another decrease reported in 2008.

The pattern is the same as other companies in the sector, reporting a significant decrease in share price and stable performance of other indicators during the period. The company was affected by rising input, hence the reduced margins. Despite regional expansion and new product development, 2008 saw the negative impact of post election violence that led to an increase in the costs of raw materials, electricity and fuel. In addition, the company had to comply with legal requirements on employee safety which increased the administration expenses in the same period.

## Mumias Sugar

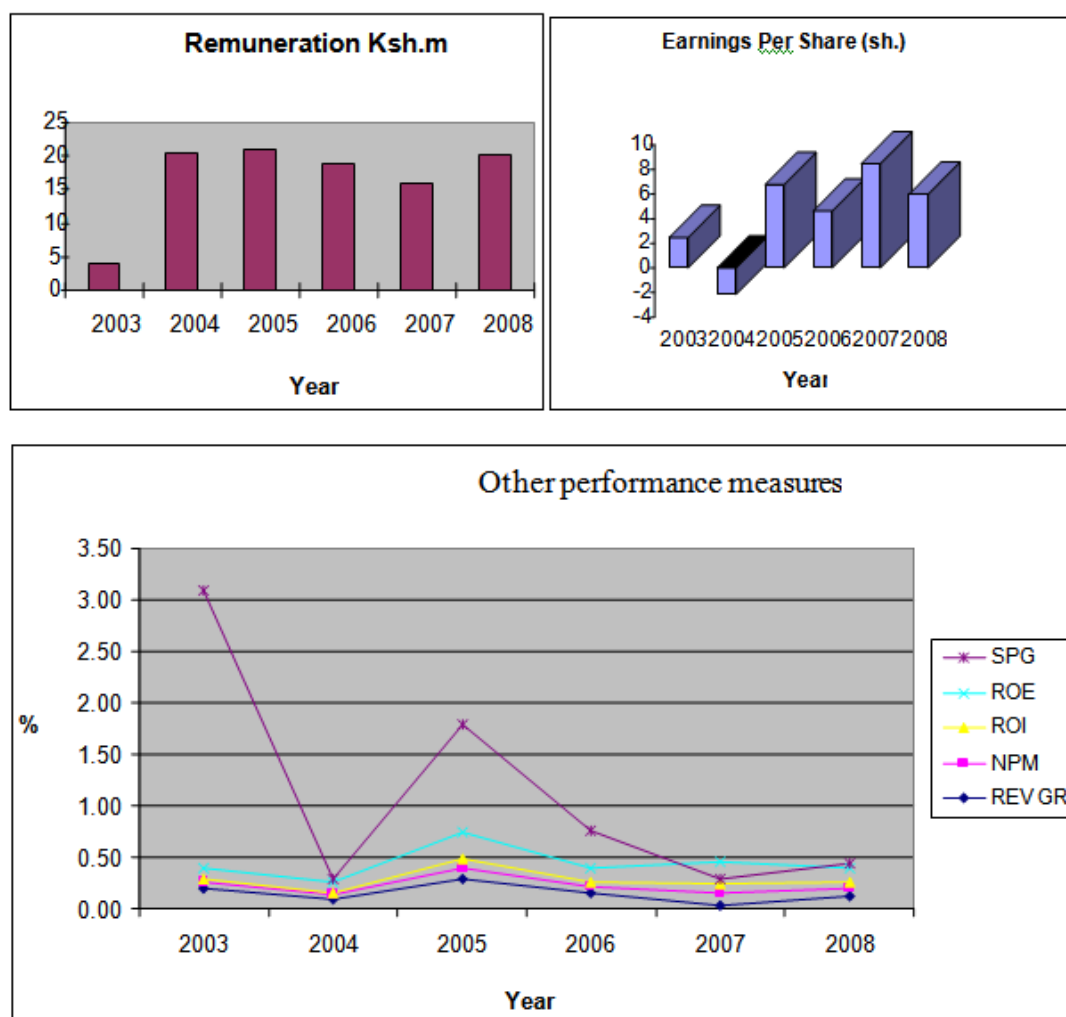


**Figure 17 - Mumias Sugar company- Directors remuneration & performance measures**

The firm reported a significant increase in remuneration in 2004 but this remained stable with a modest increase over the period to 2008. The number of directors remained the same over the period. The Earnings per Share trend has improved significantly from a negative in 2003 to the highest peak in 2006. Unfortunately the trend has reversed and there was a significant decline by the end of 2008.

The Share Price Growth had improved in 2004, but reported a significant decline in 2007, which was worse than the other performance measures. The others did not change over the period. The company reported an increase in demand for sugar with relatively stable prices. But poor infrastructure, stiff competition, industrial disputes and the negative effects of the post election violence affected the performance especially between 2007 and 2008. It is also important to note that in 2004, the company reported a profit for the first time since the early nineties.

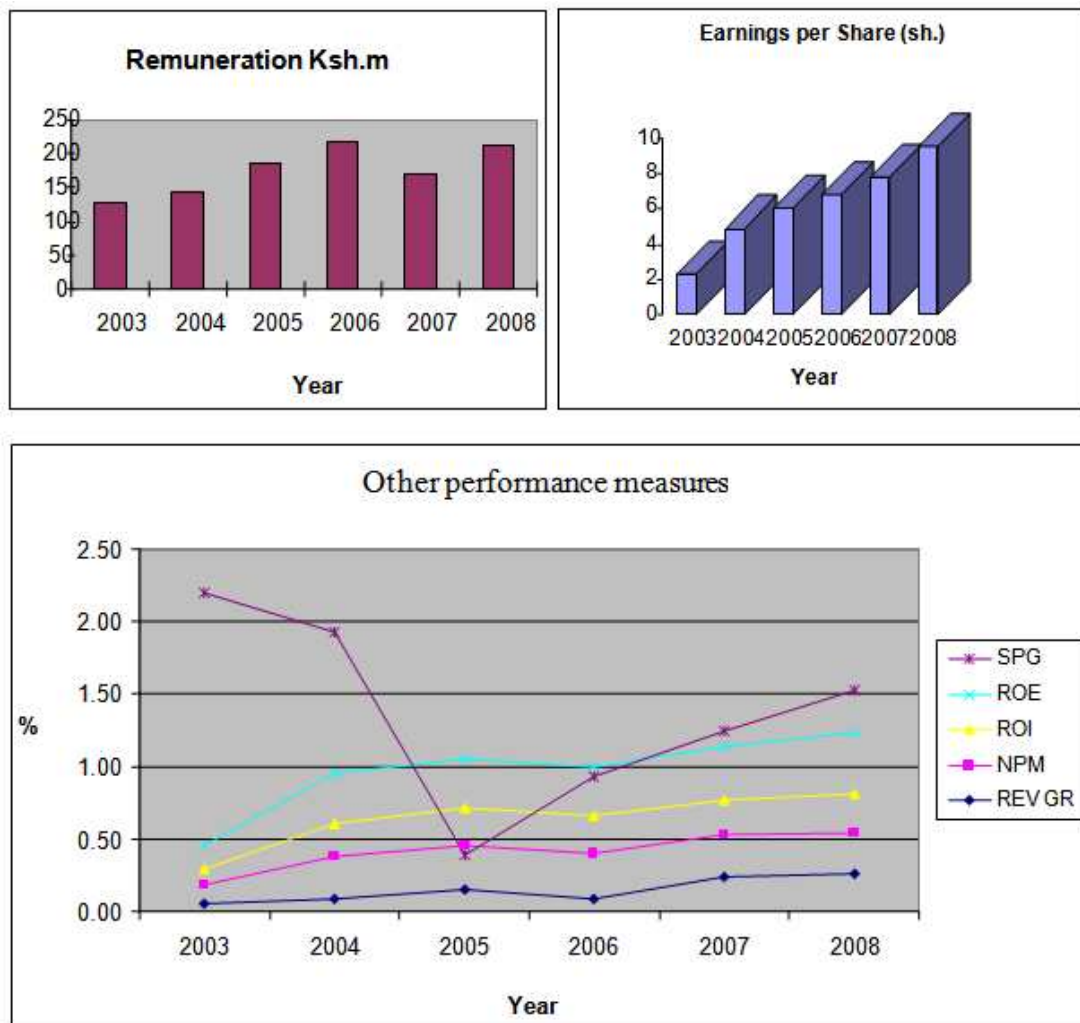
## East African Portland



**Figure 18 - East Africa Portland- Directors remuneration & performance measures**

East African Portland reported a significant increase in remuneration in 2004 with stability over the same period to 2008. The number of directors remained the same (8). There was a general increase in Earnings per Share from 2005 but mixed performance between 2005 and 2008 with a decrease in 2006 and 2008 and an increase in 2007. Apart from the Share Price Growth, most of the other performance measures remained stable over the same period. The share price was slightly volatile with a significant increase in 2005 and a decrease in 2006 and 2007. As with other cement companies, its performance was boosted by rising demand of cement and operational efficiencies.

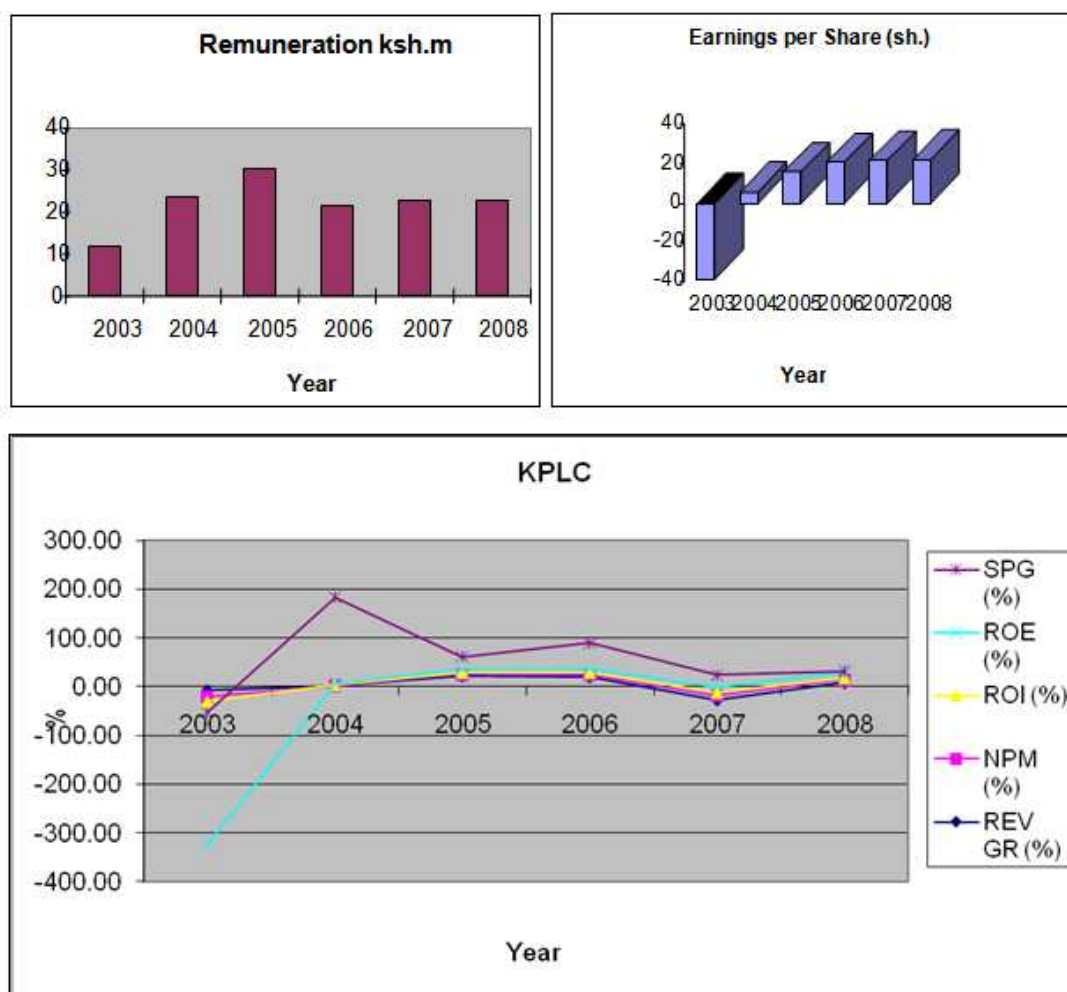
## East African Breweries



**Figure 19 - East African Breweries Limited- Directors remuneration & performance measures**

The firm reported a general increase in remuneration over time with a higher pay in 2006. As with the other companies, the number of directors remained the same over the period. The Earnings per Share has been increasing over time with a significant increase in 2008 as compared to that of 2003. All the performance measures have improved although the share price had a significant decrease in 2005, but returned to an improved trend from 2006. EABL was one of the best performing companies on the NSE in the period under study. The good performance is largely attributable to major expansion in the region, introduction of new products, acquisition of competition, and operational efficiency.

## Kenya Power and Lighting



**Figure 20 - Kenya Power and Lighting- Directors remuneration & performance measures**

The directors' remuneration has remained stable over the period under study with the highest payment made in 2005. The number of directors has also remained stable over the same period. The Earnings per Share has improved over time from a negative amount to a positive level as at 2008. However the increase was not very significant between 2006 and 2008. The company had a general improvement in performance especially for share price and Return on Equity. The rest had a modest improvement in performance. The company has reported improved performance over the period due to increased demand for electricity, renegotiation of input factors, and passing fuel cost adjustment to customers. The company has also reinforced its network supply of electricity but still faces challenges due to high transmission and distribution costs.

## Kenya National Oil

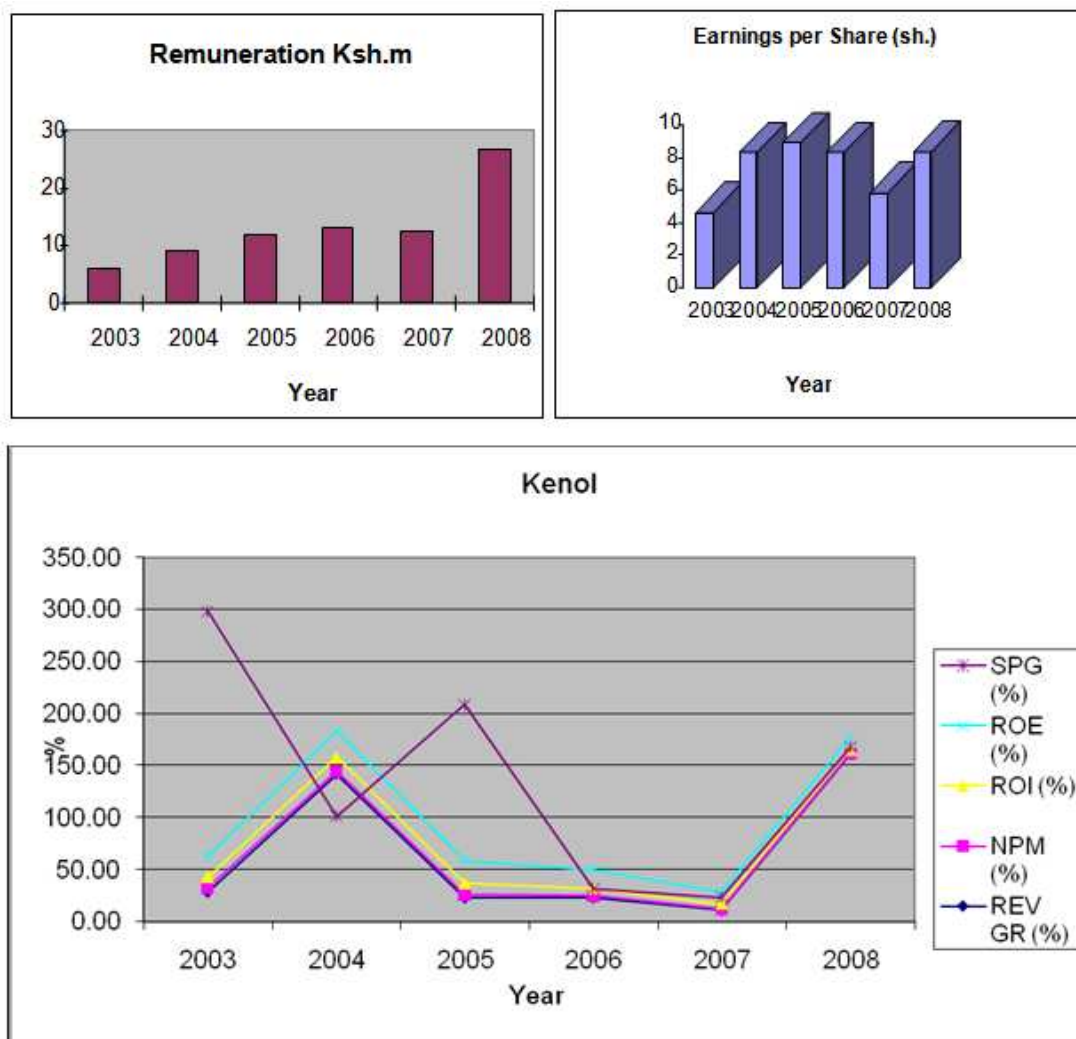
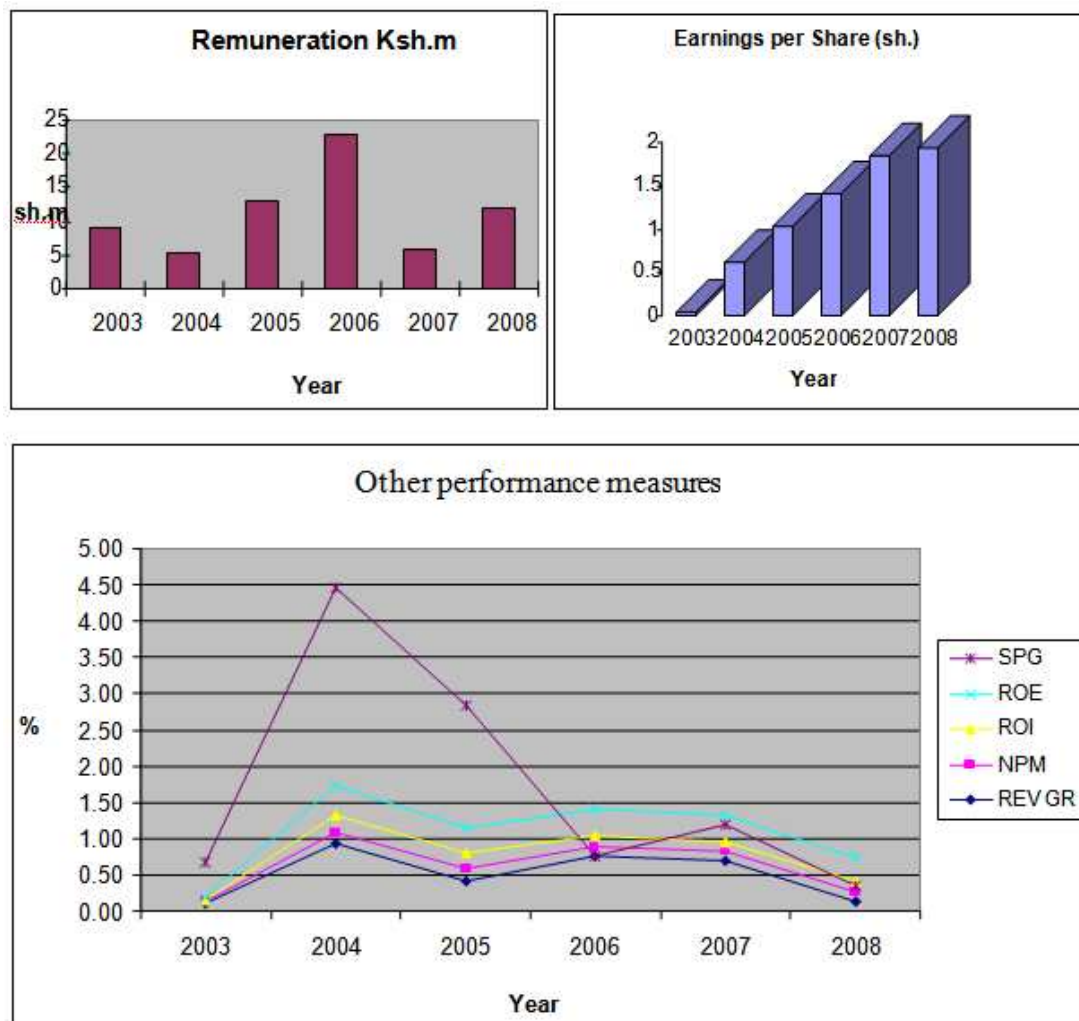


Figure 21 - Figure 4.19: Kenya National Oil – Directors remuneration & performance measures

There was a general insignificant increase in remuneration except in 2008 when the increase was significant. The number of directors remained the same, and there was no explanation of the increase. Generally, the firm has reported some stability in the earnings per share with some significant increase and decrease in 2003 and 2007.

Kenol reported a decline in other performance measures over the years to 2007 but reversed the trend in 2008. The good performance that was reported from 2003 to 2005 was due to increase in demand for fuel and increase in fuel prices. In addition the company's hedging strategies paid off. From 2005, the global fuel prices went up and due to social and media campaign, the company could not pass it to the customers. There was also stiff competition. Recoveries were made as from 2007, when the global fuel costs reduced.

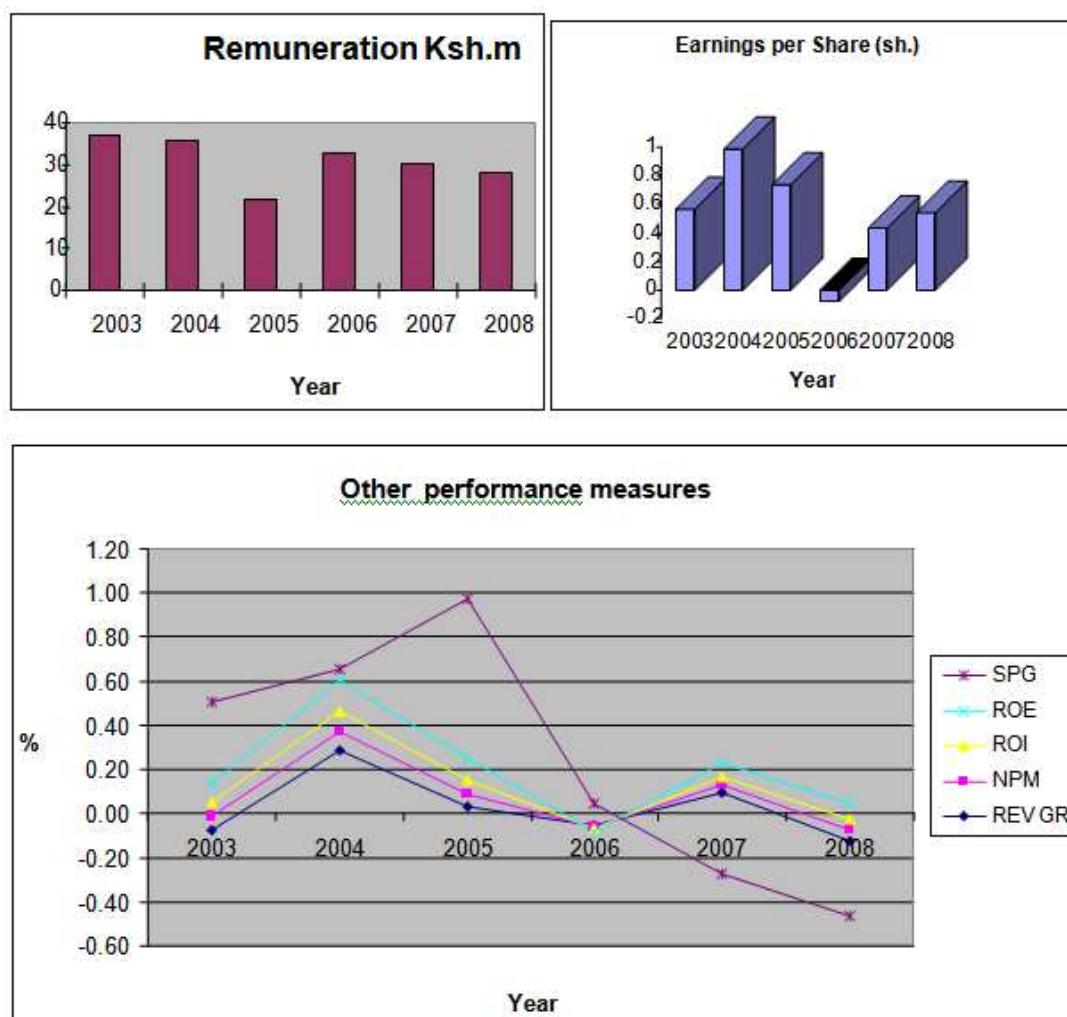
## East African Cables



**Figure 22 - East African cables – Directors remuneration & performance measures**

The directors' remuneration for the company is somehow volatile with a very significant pay in 2006 followed by another significant decline in payment in 2007. This is despite the fact that the number of directors remained the same over the years. No explanation is given for the same. The firm had a consistent increase in earnings per share with a very significant improvement recorded in 2007 and 2008. The other performance measures have declined modestly over the years with the share price reporting significant declines in 2004. The general performance is attributed to operational efficiency and expansion into foreign markets (Tanzania and Uganda) though there was an adverse effect due to the post election violence in 2008.

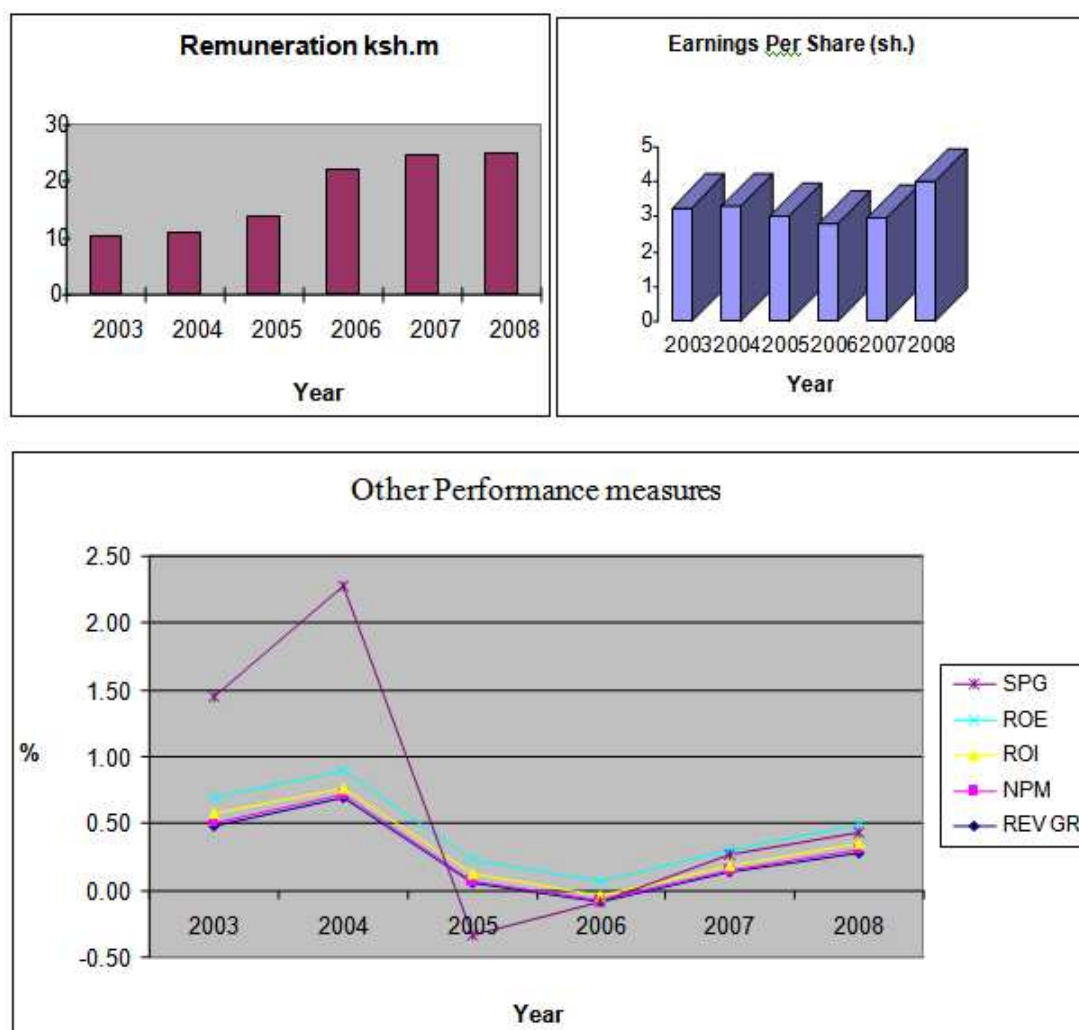
## Sameer East Africa



**Figure 23 - Sameer East Africa– Directors remuneration & performance measures**

There was a general decline in remuneration over time with higher amounts paid in 2003 and 2004. The Earnings per Share has also declined over the period with a negative Earnings Per share in 2006. Most of the performance measures have declined with the most significant decline reported in the Share Price Growth. The decline in the performance was largely attributable to stiff competition and an increase in operational expenses, especially in 2008 as a result of post election violence. The company tried some mitigation strategies, such as the change of name, increasing focus on foreign markets and aggressive marketing which paid off somehow in 2004 and 2005 and around 2006, when there was staff restructuring.

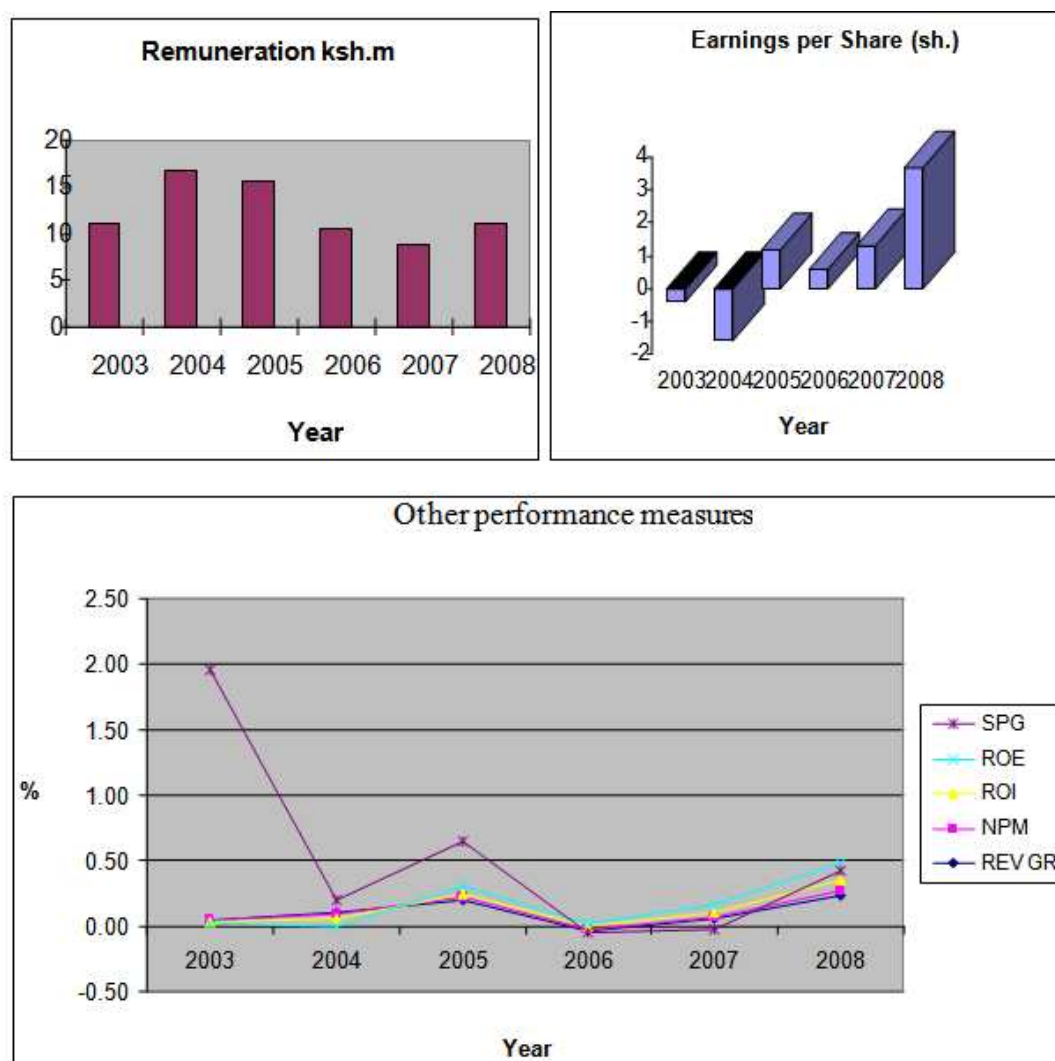
## Total Kenya Limited



**Figure 24 - Total Kenya – Directors remuneration & performance measures**

Total Kenya experienced a general increase in remuneration over the period with some stability in 2007 and 2008. The Earnings per Share generally declined from 2003 to 2007, but there was a slight improvement in 2008. All the performance measures declined again with the share price reporting a significant decline in 2005. Just like in the case of Kenya National Oil, Total Kenya performed well from 2003 to 2005 due to an increase in demand for fuel and increase in fuel prices. The company attributed the poor performance from 2004 to unfavourable market conditions for the oil sector stemming from volatility in world oil prices, production uncertainties, restrictions on importations and taxes (fuel levy). The increase in world oil prices could not be passed to consumers. From 2005 and 2006, the world oil prices reduced and the company also embarked on operational efficiency to reduce costs.

## Unga Group



**Figure 25 - Unga Group – Directors remuneration & performance measures**

The firm reported general stability in executive remuneration but there were significant increases in 2004 and 2005. The number of directors also remained relatively the same over the period. The company had a general increase in Earnings per Share from a negative position in 2004 to a positive level in 2008.

The company had a general improvement in performance by all the indicators except for share price which had a significant decline in 2003. Some factors that adversely impacted on the company's performance were the decline in turnover for human feeds and increase in cost of raw materials, shortage due to poor weather conditions, high operating costs and stiff competition. However, the company continued to introduce several products and manage operational costs in order to mitigate against an adverse operating environment.

Table 9 provides a summary of remuneration and the key performance indicators for each company.

**Table 9 - Summary Remuneration and Firm Performance – Industrial & Allied**

|                          |     | REM   | REV     | NPM    | ROI    | ROE     | SPG     | EPS   |
|--------------------------|-----|-------|---------|--------|--------|---------|---------|-------|
|                          |     | Sh.m  | GR%     | %      | %      | %       | %       | Sh.   |
| Athi River Mining        | Max | 59.2  | 48.96%  | 10.89% | 9.37%  | 23.81%  | 352.13% | 5.08  |
|                          | Min | 19.9  | 10.12%  | 1.00%  | 0.61%  | 1.89%   | -29.41% | 1.04  |
|                          | Avg | 41.15 | 27.17%  | 7.78%  | 5.99%  | 14.52%  | 100.83% | 2.75  |
| Bamburi Cement           | Max | 112   | 34.10%  | 17.23% | 21.60% | 29.43%  | 188.00% | 9.91  |
|                          | Min | 91.7  | 3.36%   | 11.07% | 7.49%  | 10.00%  | -24.60% | 2.94  |
|                          | Avg | 80.83 | 18.57%  | 14.69% | 14.65% | 20.37%  | 39.52%  | 6.51  |
| BOC Kenya                | Max | 22.4  | 35.59%  | 20.99% | 14.42% | 19.14%  | 271.96% | 13.70 |
|                          | Min | 14    | -14.68% | 15.58% | 9.72%  | 13.76%  | 0.00%   | 7.82  |
|                          | Avg | 16.23 | 11.76%  | 19.16% | 12.09% | 15.85%  | 54.31%  | 10.36 |
| British American Tobacco | Max | 179   | 23.54%  | 22.14% | 30.35% | 35.50%  | 411.11% | 17.00 |
|                          | Min | 53    | -1.77%  | 14.71% | 14.95% | 27.14%  | -29.44% | 11.40 |
|                          | Avg | 100.5 | 11.66%  | 18.64% | 20.48% | 31.29%  | 57.70%  | 13.37 |
| Crown-Berger (Kenya)     | Max | 24.5  | 44.94%  | 5.09%  | 6.36%  | 9.93%   | 407.14% | 3.15  |
|                          | Min | 8.4   | -14.67% | 1.17%  | 1.44%  | 3.41%   | -49.50% | 1.20  |
|                          | Avg | 14.93 | 15.76%  | 3.49%  | 4.11%  | 7.56%   | 66.99%  | 2.26  |
| Mumias Sugar             | Max | 55    | 28.37%  | 13.51% | 13.58% | 21.22%  | 170.72% | 2.94  |
|                          | Min | 6.2   | -10.40% | -2.82% | -2.38% | -4.42%  | -57.10% | -0.42 |
|                          | Avg | 42.47 | 8.04%   | 9.16%  | 8.83%  | 13.57%  | 69.31%  | 1.69  |
| EA Portland Cement       | Max | 21    | 28.73%  | 11.95% | 8.56%  | 26.99%  | 270.00% | 8.49  |
|                          | Min | 3.9   | 3.59%   | 4.61%  | 2.57%  | 10.50%  | -16.67% | -2.13 |
|                          | Avg | 16.72 | 14.72%  | 7.98%  | 5.42%  | 16.01%  | 66.81%  | 4.36  |
| East African Breweries   | Max | 216   | 25.58%  | 30.66% | 27.62% | 41.52%  | 173.94% | 9.55  |
|                          | Min | 125.3 | 5.45%   | 12.90% | 11.36% | 15.61%  | -66.52% | 2.29  |
|                          | Avg | 175.9 | 14.72%  | 26.61% | 22.91% | 32.83%  | 39.60%  | 6.22  |
| Kenya Power and Lighting | Max | 30.3  | 21.52%  | 10.84% | 5.60%  | 11.91%  | 269.94% | 22.30 |
|                          | Min | 11.9  | -28.06% | -13.2% | -9.71% | -293.3% | 2.39%   | -38.5 |
|                          | Avg | 22.03 | 2.54%   | 2.53%  | 1.56%  | -42.2%  | 91.71%  | 8.01  |
| Kenya Oil                | Max | 26.7  | 160.59% | 3.73%  | 13.44% | 24.70%  | 235.80% | 8.96  |
|                          | Min | 5.8   | 11.30%  | 0.86%  | 4.17%  | 10.58%  | -81.43% | 4.65  |
|                          | Avg | 13.15 | 64.94%  | 2.12%  | 8.23%  | 17.88%  | 45.26%  | 7.42  |

|                     |     |       |        |        |        |        |         |       |
|---------------------|-----|-------|--------|--------|--------|--------|---------|-------|
| East African Cables | Max | 22.7  | 92.76% | 18.33% | 25.20% | 39.12% | 273.63% | 1.94  |
| Sameer Group        | Min | 5.3   | 10.31% | 2.10%  | 2.53%  | 3.61%  | -64.96% | 0.05  |
|                     | Avg | 11.32 | 50.44% | 12.21% | 15.19% | 31.00% | 62.41%  | 1.15  |
|                     | Max | 36.8  | 28.84% | 8.41%  | 9.21%  | 13.67% | 72.00%  | 0.99  |
|                     | Min | 21.4  | -      | -0.69% | -0.66% | -1.19% | -50.41% | -0.08 |
|                     | Avg | 30.78 | 12.74% | 2.56%  | 4.73%  | 4.98%  | 7.32%   | 4.35% |
| Total Kenya         | Max | 25    | 69.53% | 2.74%  | 6.54%  | 14.01% | 137.74% | 4.02  |
|                     | Min | 10.1  | -8.61% | 1.51%  | 3.16%  | 10.40% | -56.61% | 2.78  |
|                     | Avg | 17.82 | 26.01% | 1.80%  | 4.85%  | 12.03% | 22.09%  | 3.24  |
| Unga Group          | Max | 16.7  | 23.14% | 3.96%  | 7.86%  | 12.62% | 193.90% | 3.67  |
|                     | Min | 8.8   | -3.35% | -2.00% | -2.96% | -6.31% | -18.38% | -1.62 |
|                     | Avg | 12.23 | 10.01% | 0.96%  | 2.13%  | 3.27%  | 36.06%  | 0.78  |

The table shows that East Africa Breweries paid the highest remuneration to its directors. However companies in this sector performed relatively well and there was no exceptional company.

Table 10 summarises the average remuneration and performance for the sector over the six years.

**Table 10 - Annual remuneration and firm performance for Industrial and allied sector**

|           | 2003    | 2004   | 2005   | 2006   | 2007   | 2008   | Average |
|-----------|---------|--------|--------|--------|--------|--------|---------|
| RE- sh. m | 27.95   | 36.68  | 42.25  | 48.11  | 47.82  | 57.29  | 43.35   |
| REV GR -% | 8.76%   | 33.08% | 20.62% | 13.40% | 23.19% | 23.32% | 20%     |
| NPM -%    | 5.96%   | 9.81%  | 11.22% | 9.43%  | 10.18% | 9.42%  | 9%      |
| ROI -%    | 5.46%   | 10.55% | 11.58% | 8.72%  | 10.13% | 9.69%  | 9%      |
| ROE -%    | -11.25% | 16.47% | 19.13% | 15.65% | 18.88% | 18.42% | 13%     |
| SPG -%    | 212.13% | 52.33% | 60.33% | 24.08% | -9.95% | -14.5% | 54%     |
| EPS- sh.  | -0.01   | 3.57   | 5.70   | 6.05   | 7.00   | 7.10   | 4.90    |

The average remuneration has also been increasing over the period although the sector has experienced some stability in profitability measures. The share price has been declining over the years.

Table 11 summarises the regression results for individual companies in the sector.

**Table 11 - Individual companies' regression - Industrial and Allied**

|                          | Remuneration Vs |            |         |         |         |          |           |
|--------------------------|-----------------|------------|---------|---------|---------|----------|-----------|
|                          |                 | REV GR (%) | NPM (%) | ROI (%) | ROE (%) | SPG (%)  | EPS (sh.) |
| Athi River Mining        | $\alpha$        | 32.86      | 38.61   | 37.95   | 29.7    | 48.3     | 14.06     |
|                          | P( $\alpha$ )   | 0.138      | 0.124   | 0.117   | 0.125   | 0.004    | 0.080     |
|                          | $\beta$         | 0.305      | 0.327   | 0.533   | 0.7889  | -0.07073 | 9.858     |
|                          | P( $\beta$ )    | 0.633      | 0.896   | 0.863   | 0.445   | 0.22     | 0.007     |
|                          | R <sup>2</sup>  | 6.20%      | 0.50%   | 0.80%   | 15.20%  | 34.50%   | 86.80%    |
|                          | DW              | 0.64       | 0.45    | 0.47    | 1.06    | 1.1      | 2.1       |
| Bamburi Cement           | $\alpha$        | 64.6       | 52.6    | 42.7    | 41.86   | 97.9     | 51.1      |
|                          | P( $\alpha$ )   | 0.002      | 0.336   | 0.028   | 0.013   | 0.00     | 0.003     |
|                          | $\beta$         | 1.455      | 2.655   | 3.34    | 2.44    | -0.15    | 6.225     |
|                          | P( $\beta$ )    | 0.029      | 0.457   | 0.16    | .006    | .096     | .006      |
|                          | R <sup>2</sup>  | 73%        | 14.4%   | 80%     | 87%     | 54%      | 88%       |
|                          | DW              | 2.10       | 0.64    | 2.1     | 2.4     | 1.5      | 2.2       |
| BOC Kenya                | $\alpha$        | 16.3       | 10.49   | 16.9    | 19.3    | 14.8     | 20.6      |
|                          | P( $\alpha$ )   | 0.001      | 0.508   | 0.217   | 0.167   | 0.000    | 0.053     |
|                          | $\beta$         | -0.01188   | 0.2996  | -0.0556 | -0.1907 | 0.026984 | -0.4232   |
|                          | P( $\beta$ )    | 0.91       | 0.71    | 0.956   | 0.803   | 0.018    | 0.587     |
|                          | R <sup>2</sup>  | 0.40%      | 3.80%   | 0.10%   | 1.70%   | 79.00%   | 8.00%     |
|                          | DW              | 1.6        | 1.52    | 1.6     | 1.8     | 1.7      | 1.97      |
| British American Tobacco | $\alpha$        | 81.89      | 269.6   | 157.2   | -94     | 108      | -175.9    |
|                          | P( $\alpha$ )   | 0.060      | 0.048   | .073    | .637    | .005     | 0.028     |
|                          | $\beta$         | 1.6        | -9.071  | -2.783  | 6.223   | -0.1331  | 20.69     |
|                          | P( $\beta$ )    | 0.496      | 0.148   | 0.413   | 0.35    | 0.3      | 0.006     |
|                          | R <sup>2</sup>  | 12.30%     | 44.50%  | 17.30%  | 21.90%  | 26.10%   | 87.70%    |
|                          | DW              | 0.78       | 1.48    | 1.008   | 0.49    | 0.78     | 2.14      |
| Crown-Berger (Kenya)     | $\alpha$        | 15.37      | 19.7    | 21.3    | 20.9    | 15.9     | 14.1      |
|                          | P( $\alpha$ )   | 0.16       | 0.057   | 0.048   | 0.094   | 0.007    | 0.205     |
|                          | $\beta$         | -0.0282    | -1.377  | -1.558  | -0.788  | -0.0139  | 0.355     |
|                          | P               | 0.859      | 0.522   | 0.417   | 0.549   | 0.49     | 0.932     |
|                          | R <sup>2</sup>  | 0.90%      | 10.90%  | 17.00%  | 9.70%   | 12.60%   | 0.20%     |
|                          | DW              | 0.52       | 1.23    | 1.18    | 1.031   | 1.06     | 0.667     |
| Mumias Sugar             | $\alpha$        | 39.4       | 17.3    | 17.9    | 18.6    | 43       | 25.2      |
|                          | P( $\alpha$ )   | 0.014      | 0.032   | 0.064   | 0.054   | 0.013    | 0.06      |
|                          | $\beta$         | 0.3722     | 2.7421  | 2.7773  | 1.7574  | -0.00785 | 10.217    |
|                          | P( $\beta$ )    | 0.579      | 0.005   | 0.015   | 0.015   | 0.93     | 0.094     |
|                          | R <sup>2</sup>  | 8.30%      | 88.30%  | 80.40%  | 80.60%  | 0.20%    | 54.40%    |
|                          | DW              | 0.68       | 1.8     | 1.25    | 0.954   | 0.958    | 1.21      |
| EA Portland Cement       | $\alpha$        | 17.7       | 12.9    | 11.7    | 10.98   | 20.018   | 15.9      |
|                          | P( $\alpha$ )   | 0.045      | 0.22    | 0.179   | 0.233   | 0.001    | 0.029     |
|                          | $\beta$         | -0.0674    | 0.474   | 0.912   | 0.3591  | -0.04941 | 0.181     |
|                          | P( $\beta$ )    | 0.863      | 0.679   | 0.501   | 0.476   | 0.046    | 0.844     |
|                          | R <sup>2</sup>  | 0.80%      | 4.70%   | 12.00%  | 13.40%  | 67.30%   | 1.10%     |
|                          | DW              | 1.4        | 1.81    | 2.08    | 2.1     | 1.83     | 1.6       |

|                        |                |          |         |         |         |         |         |
|------------------------|----------------|----------|---------|---------|---------|---------|---------|
| East African Breweries | $\alpha$       | 143.6    | 73.7    | 56.8    | 77.3    | 189     | 101     |
| Kenya Power & Lighting | P( $\alpha$ )  | 0.01     | 0.226   | 0.229   | 0.181   | 0.000   | 0.022   |
|                        | $\beta$        | 2.192    | 3.83    | 5.198   | 3.002   | -0.3356 | 12.043  |
|                        | P( $\beta$ )   | 0.308    | 0.113   | 0.038   | 0.101   | 0.07    | 0.045   |
|                        | R <sup>2</sup> | 25.40%   | 50.50%  | 70.00%  | 53.00%  | 60.20%  | 67.60%  |
|                        | DW             | 2.08     | 2.07    | 2.06    | 2.04    | 2.01    | 2.06    |
|                        | $\alpha$       | 21.73    | 20.68   | 2073    | 23.79   | 25.7    | 20.4    |
|                        | P( $\alpha$ )  | 0.001    | 0.000   | 0.000   | 0.037   | 0.001   | 0.000   |
|                        | $\beta$        | 0.1304   | 0.5307  | 0.8189  | 0.04016 | -0.0400 | 0.19442 |
|                        | P( $\beta$ )   | 0.42     | 0.092   | 0.061   | 0.037   | 0.101   | 0.068   |
|                        | R <sup>2</sup> | 16.80%   | 54.90%  | 62.40%  | 70.10%  | 53.00%  | 60.70%  |
| Kenya Oil              | DW             | 1.9      | 1.72    | 1.88    | 2.04    | 1.5     | 1.899   |
|                        | $\alpha$       | 9.29     | 24.71   | 23.5    | 28.8    | 14.2    | -0.93   |
|                        | P( $\alpha$ )  | 0.078    | 0.006   | 0.02    | 0.027   | 0.012   | 0.95    |
|                        | $\beta$        | 0.0594   | -5.45   | -1.2636 | -0.8777 | -0.0234 | 1.899   |
|                        | P( $\beta$ )   | 0.249    | 0.049   | 0.146   | 0.127   | 0.439   | 0.357   |
|                        | R <sup>2</sup> | 31.30%   | 66.10%  | 44.80%  | 48.00%  | 15.50%  | 21.30%  |
|                        | DW             | 0.79     | 2.17    | 1.96    | 2.08    | 1.36    | 0.63    |
|                        | $\alpha$       | 11.53    | 8.5     | 12.2    | 10.2    | 12.87   | 9.22    |
|                        | P( $\alpha$ )  | 0.105    | 0.32    | 0.155   | 0.261   | 0.01    | 0.177   |
|                        | $\beta$        | -0.00424 | 0.2304  | -0.0561 | 0.0349  | -0.0247 | 1.828   |
| East African Cables    | P( $\beta$ )   | 0.966    | 0.706   | 0.899   | 0.889   | 0.296   | 0.689   |
|                        | R <sup>2</sup> | 0.10%    | 4.00%   | 0.50%   | 0.60%   | 26.50%  | 4.40%   |
|                        | DW             | 2.08     | 2.04    | 2.35    | 2.05    | 2.1     | 2.07    |
|                        | $\alpha$       | 30.5     | 30.3    | 30.1    | 30.8    | 30.8    | 31.19   |
|                        | P( $\alpha$ )  | 0.00     | 0.004   | 0.004   | 0.003   | 0.00    | 0.003   |
|                        | $\beta$        | 0.0846   | 0.1112  | 0.1369  | -0.0132 | -0.0204 | -0.781  |
|                        | P              | 0.668    | 0.908   | 0.88    | 0.983   | 0.742   | 0.926   |
|                        | R <sup>2</sup> | 5.10%    | 0.40%   | 0.60%   | 0.00%   | 3.00%   | 0.20%   |
|                        | DW             | 2        | 2.02    | 2.2     | 2.01    | 1.85    | 2       |
|                        | $\alpha$       | 21.6     | 35.7    | 39.7    | 26.2    | 19.1    | 11      |
| Total Kenya            | P( $\alpha$ )  | 0.003    | 0.023   | 0.016   | 0.456   | 0.002   | 0.691   |
|                        | $\beta$        | -0.14686 | -9.937  | -4.51   | -0.682  | -0.0567 | 2.096   |
|                        | P( $\beta$ )   | 0.195    | 0.137   | 0.087   | 0.807   | 0.225   | 0.805   |
|                        | R <sup>2</sup> | 37.70%   | 46.30%  | 55.90%  | 1.70%   | 34.00%  | 1.70%   |
|                        | DW             | 0.89     | 1.09    | 0.733   | 0.322   | 1.3     | 0.414   |
|                        | $\alpha$       | 10.9     | 13      | 13.06   | 13      | 12.2    | 12.9    |
|                        | P( $\alpha$ )  | 0.005    | 0.001   | 0.001   | 0.002   | 0.002   | 0.001   |
|                        | $\beta$        | 0.1259   | -0.7509 | -0.3916 | -0.2301 | 0.00081 | -0.826  |
|                        | P              | 0.427    | 0.321   | 0.345   | 0.334   | 0.969   | 0.342   |
|                        | R <sup>2</sup> | 16.30%   | 24.20%  | 22.20%  | 23.20%  | 0.00%   | 22.50%  |
| Unga Group             | DW             | 1.067    | 1.88    | 1.8     | 1.8     | 1.39    | 1.8     |

The main highlight for the sector is Bamburi which has shown a significant positive relationship between executive remuneration and firm performance for all the indicators except that of share price which is negative and significant. The same case applies for Athi River Mining, however the relationship is not significant. Crown

Berger and Total Kenya have reported a negative relationship for nearly all the performance indicators but the relations are not significant. For this sector we also fail to reject the null hypothesis and conclude that there is no evidence of significant positive relationship between firm performances for each of the companies

Table 12 summarises the regression results for the entire sector.

**Table 12 Summary Regression – Industrial and Allied  
Remuneration Vs**

|                 | REV GR (%) | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
|-----------------|------------|---------|---------|---------|---------|-----------|
| $\alpha$        | 46.3       | 5.95    | 3.9     | 38.9    | 47      | 35        |
| P( $\alpha$ )   | 0.00       | 0.312   | 0.543   | 0.00    | 0.00    | 0.000     |
| $\beta$         | -0.14      | 3.97    | 4.2     | 0.33    | -0.06   | 1.69      |
| P( $\beta$ )    | 0.434      | 0.00    | 0.00    | 0.26    | 0.162   | 0.024     |
| R <sup>2</sup>  | 7%         | 47%     | 43.6%   | 5.9%    | 2.4%    | 6%        |
| DW <sup>8</sup> | 2.1        | 2.01    | 1.99    | 2.04    | 2.06    | 2.08      |

Revenue Growth and Share Price Growth show a negative relationship with remuneration, while the remainder show a positive relationship. Only Net Profit Margin, Return on Investment and Earnings per Share are significant. As in the other cases, for the industrial sector, we fail to reject the null hypothesis and also conclude that there is no positive significant relationship between executive remuneration and firm performance.

<sup>8</sup> For the sector analysis the where n=84 and k=1 the DW factors lie between 1.61 and 1.66 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

#### 4.2.4 Finance and Investments

This sector reported a general increase in remuneration and was slightly better in terms of performance as compared to the other sectors. For most of the banks the good performance was attributable to good macro- economic environment, increased lending to the private sector, good management of loans and improvement of the quality of the loans such that loan loss provisions were reduced. Figure 26 to 35 summarises the trends in remuneration, Earnings per Share and the other performance indicators.

The average remuneration, other performance measures and regression results are also summarised in table 13 to 16.

##### Barclays Bank

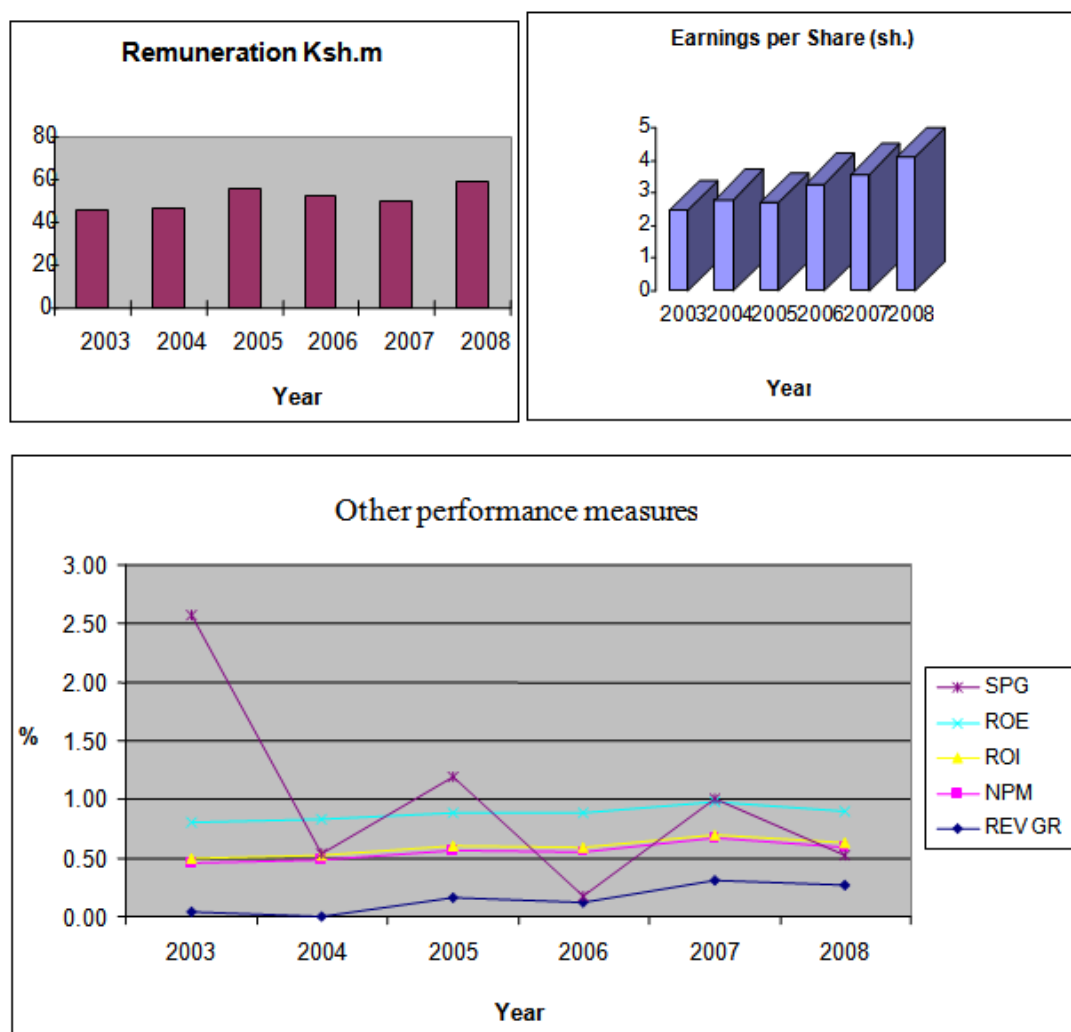
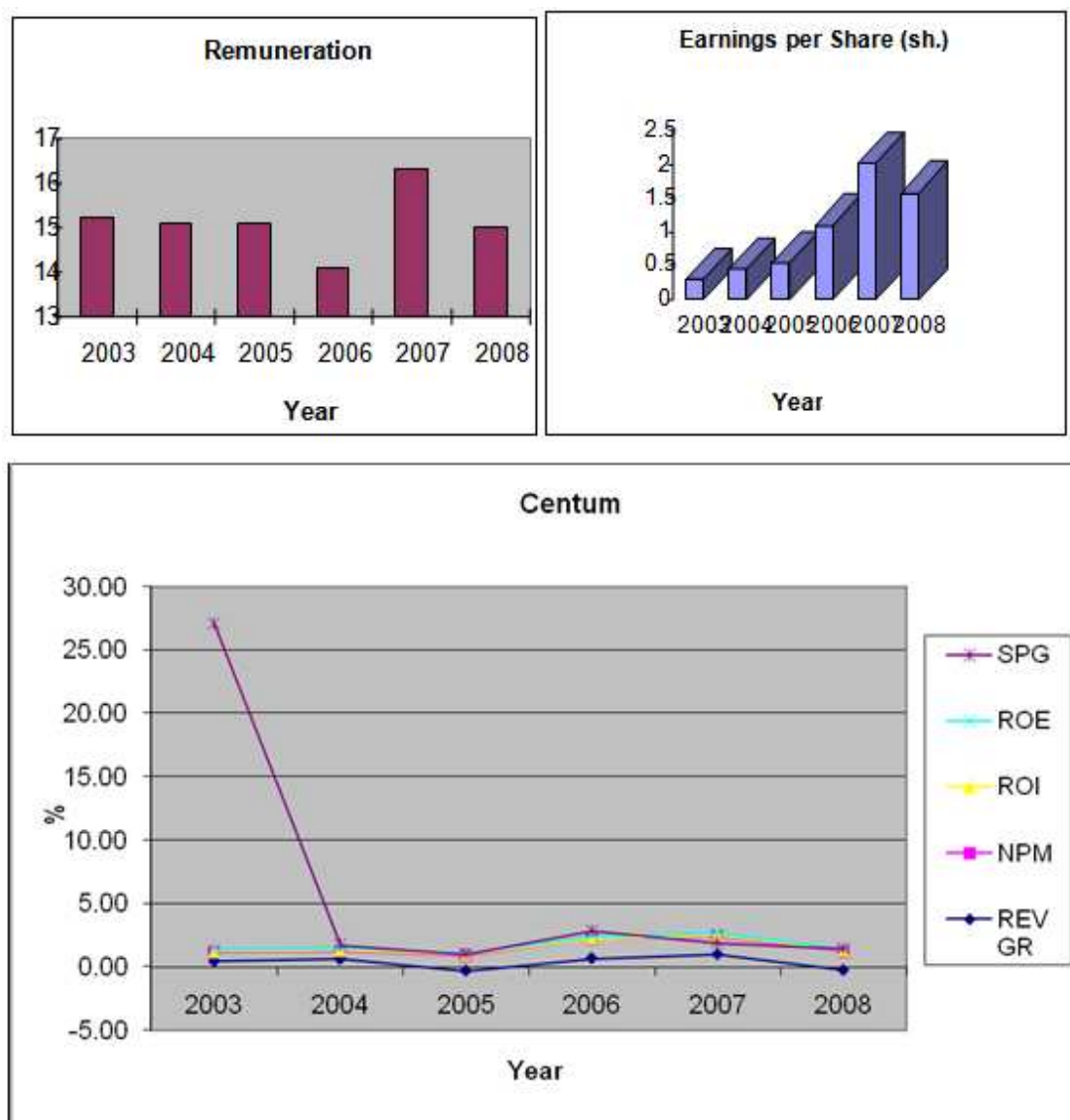


Figure 26 - Barclays Bank – Directors remuneration & performance measures.

Barclays bank reported a modest increase in executive pay with the pay in 2008 not too significant as compared to that of 2003. There was a general increase in earnings per share over the six years which shows a pattern of consistent increase.

Except for the share price, the other performance measures also reported an increase over time with the best measure being return on equity. The bank embarked also on an expansion strategy and introduced new products.

## Centum

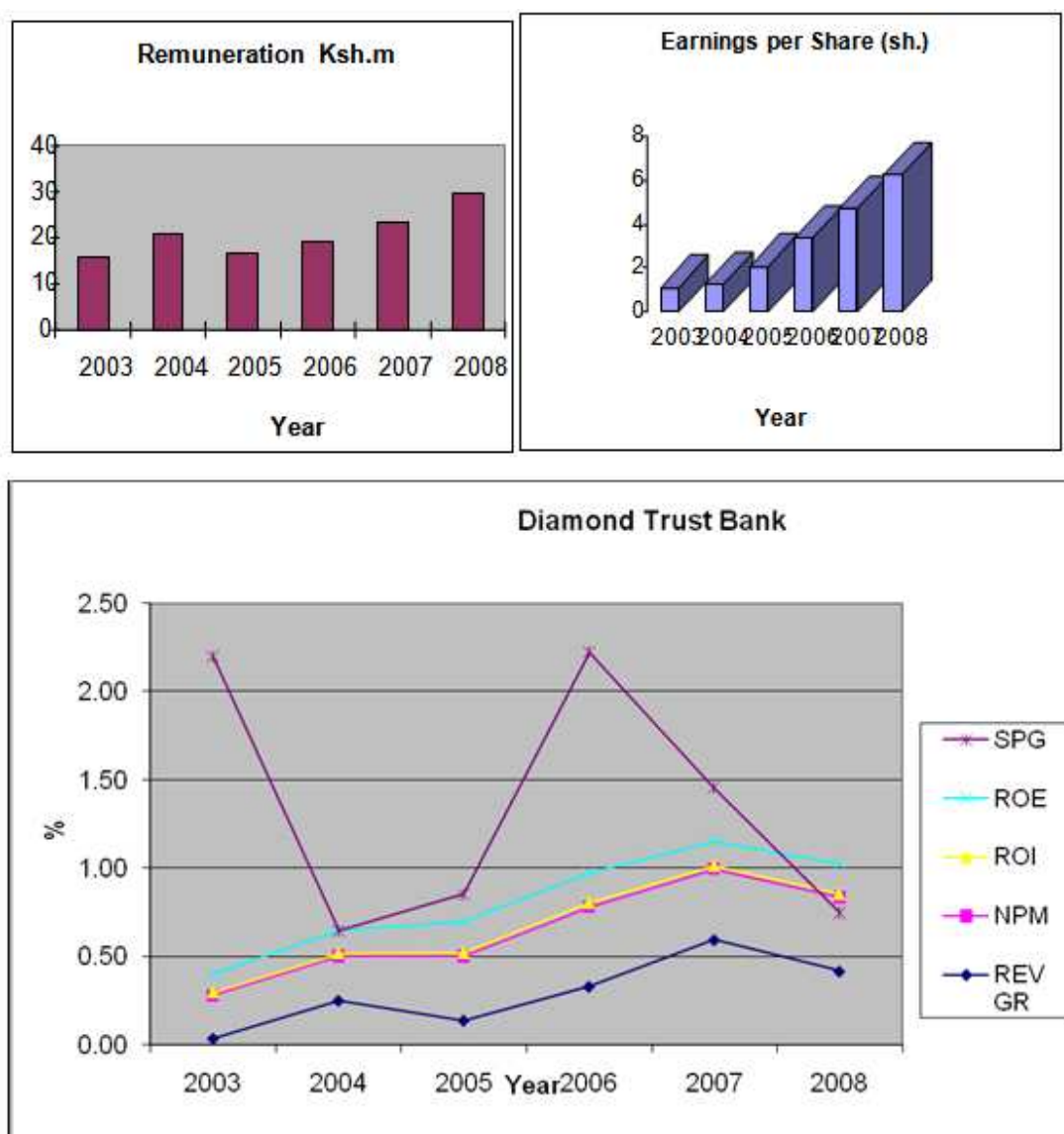


**Figure 27 - Centum – Directors remuneration & performance measures**

Centum reported a stable executive remuneration with only a significant pay made in 2007. The Earnings per Share rose significantly from 2003 to 2007 but had a small

decline in 2008. There was a significant decline in share price in 2004 just like in most companies, but the other performance measures remained stable with no much improvement. The company's performance is largely tied to the values of the investments and hence the performance shows a marginal gain in the values of investments and investment income.

### Diamond Trust Bank



**Figure 28 - Diamond Trust Bank – Directors remuneration & performance measures**

Diamond trust bank reported a general increase in remuneration and the payment made in 2008 was the highest. The Earnings per Share showed a consistent increase, with the Earnings per Share of 2008 being more significant than that of 2003.

The bank also reported a general improvement in performance for all the performance measures except for the share price, which has a high volatility with a significant decrease in 2004, followed by an increase in 2006. The banks good performance was also attributable to expansion and introduction of new products.

## Housing Finance

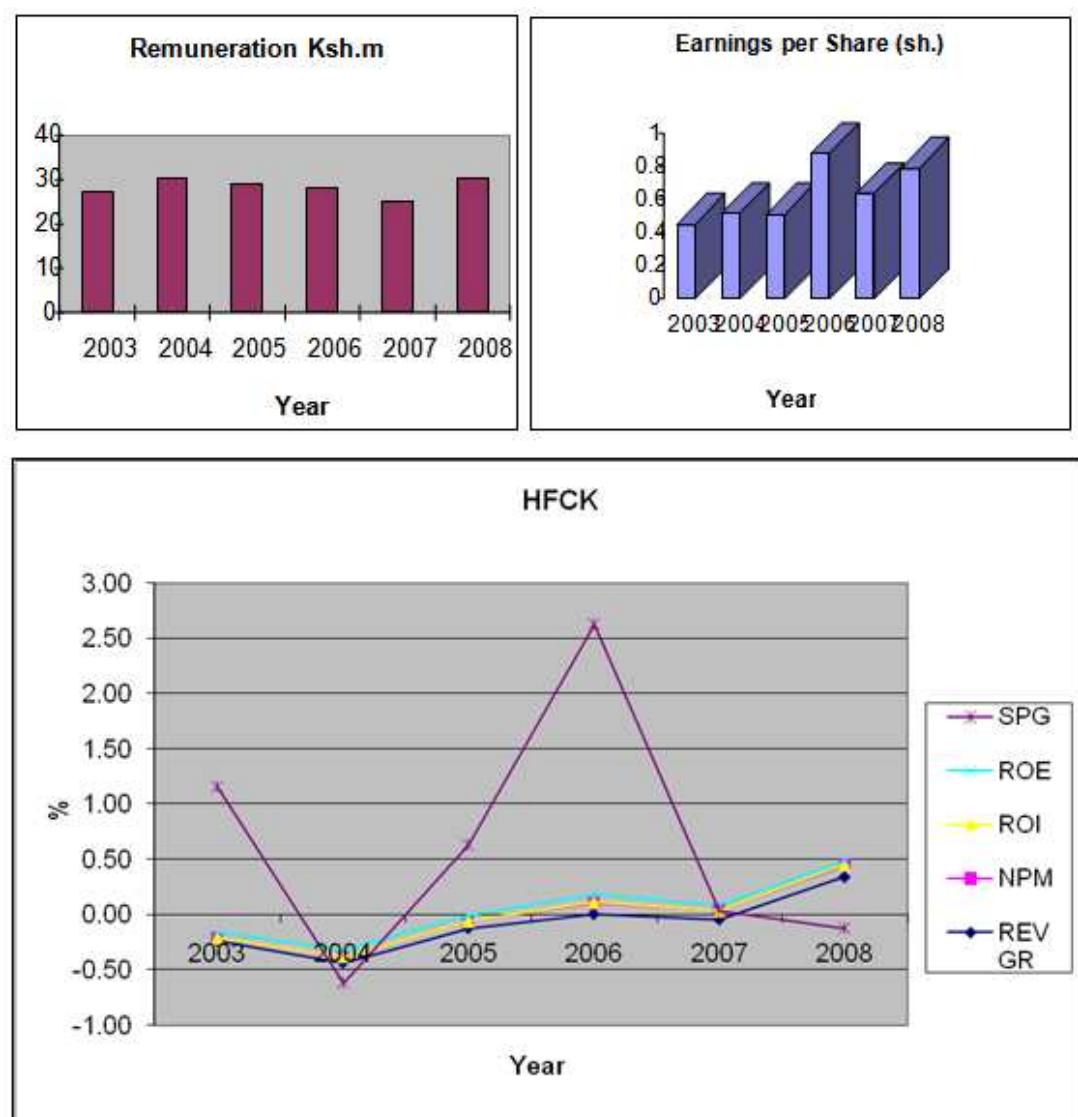
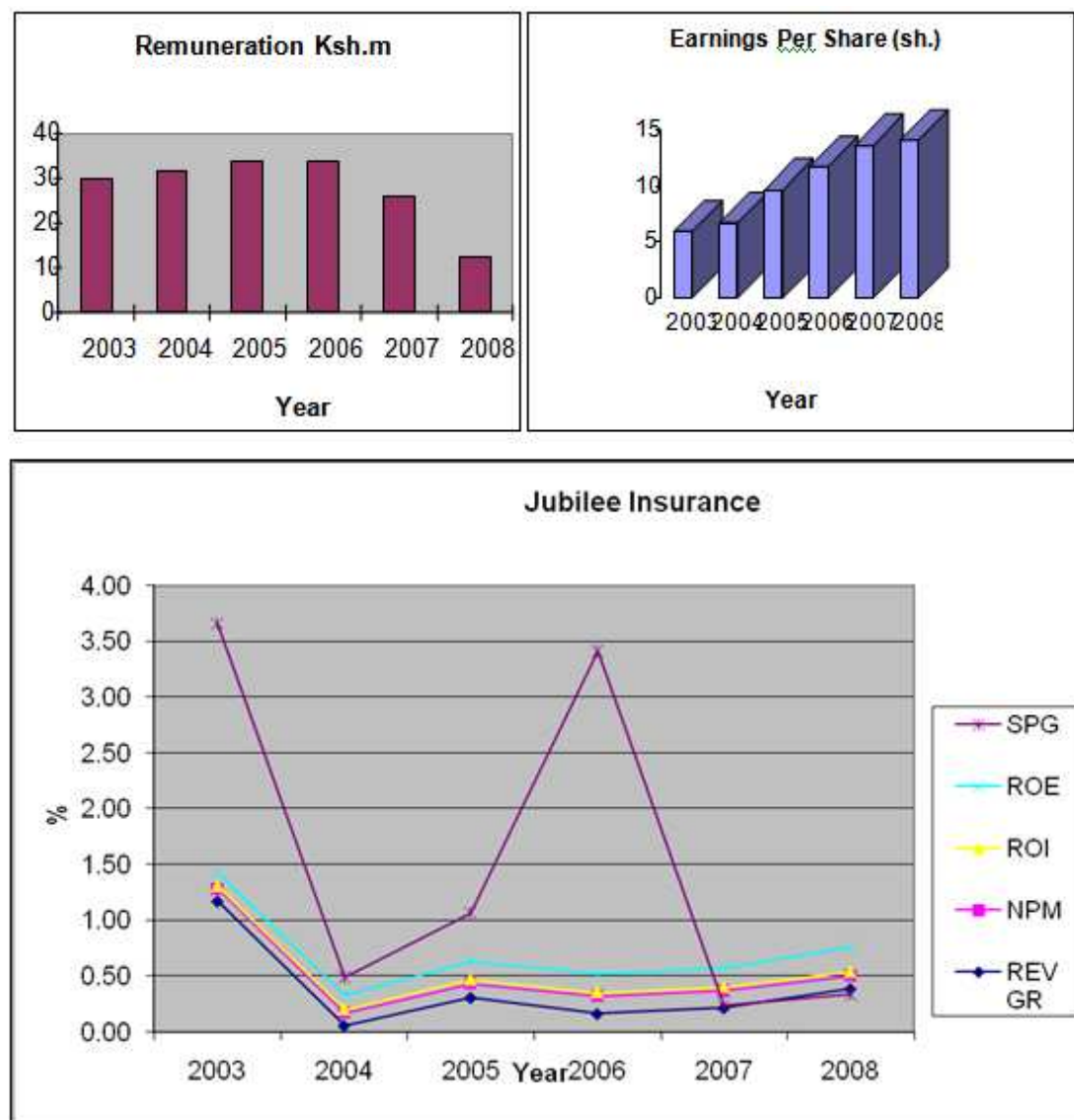


Figure 29 - Housing Finance Company – Directors remuneration & performance measures

The executive remuneration of HFCK was relatively the same throughout the entire period. The Earnings per Share showed a general increase over the period under study with a minor decline in 2007. The overall performance of the bank improved but this was modest except for the Share Price Growth that was volatile as the case for other

companies. Housing Finance has reported good performance over the period due to increased demand for mortgages (indirectly, an increase in demand for housing).

### Jubilee Insurance

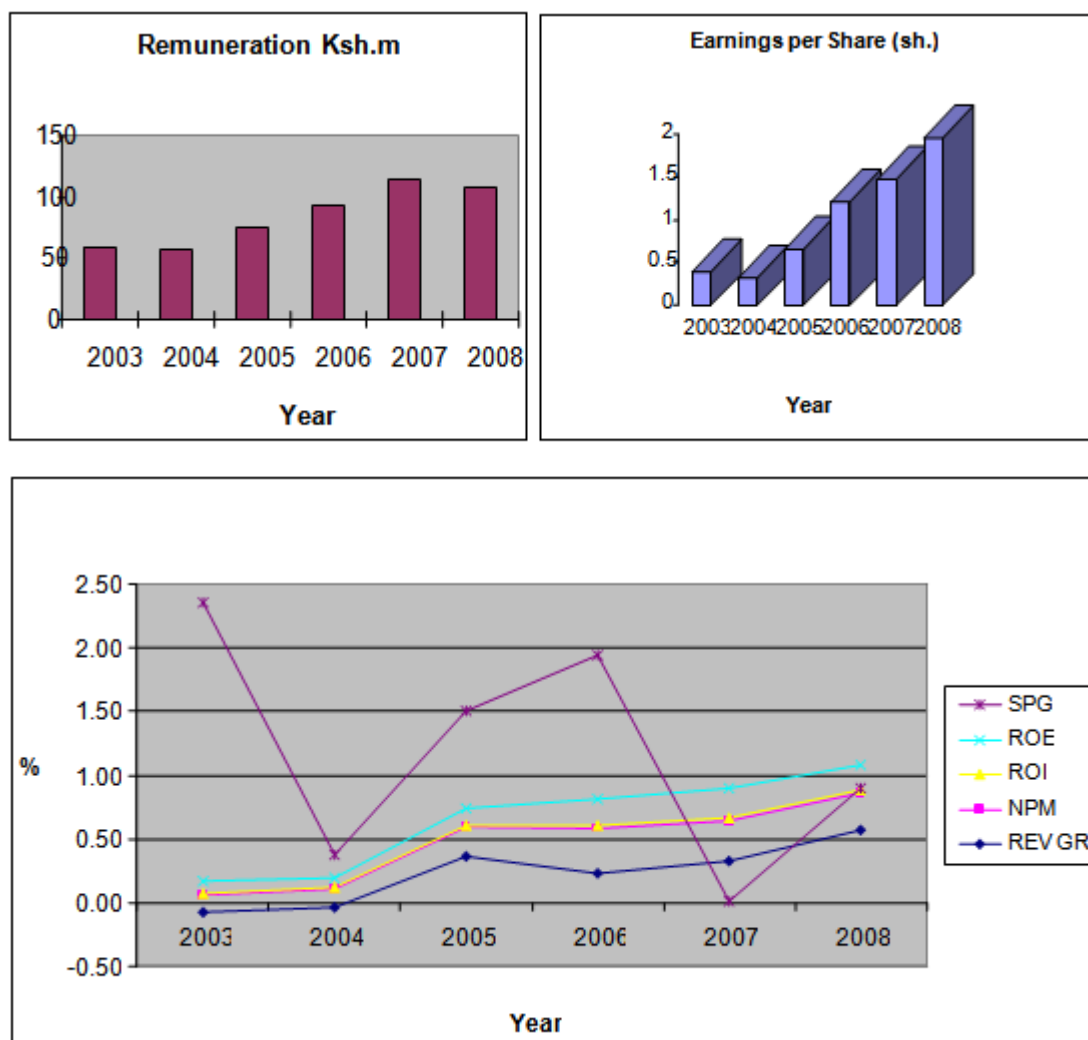


**Figure 30 - Jubilee Insurance – Directors remuneration & performance measures**

The executive remuneration for Jubilee Insurance initially increased till 2006, but then started declining from 2007, which is a slight departure as compared to the other companies in the same sector. The number of directors remained the same. The Earnings Per Share has been increasing consistently, and was very high in 2008 as compared to that of 2003. Unfortunately, the other performance measures declined initially in 2004 but have shown some improvement though not at the same level as that in 2003. The general increase in performance from 2004 was due to expansion

into foreign markets, growth in market at local and international level, and favourable performance of the stock market (Investment income).

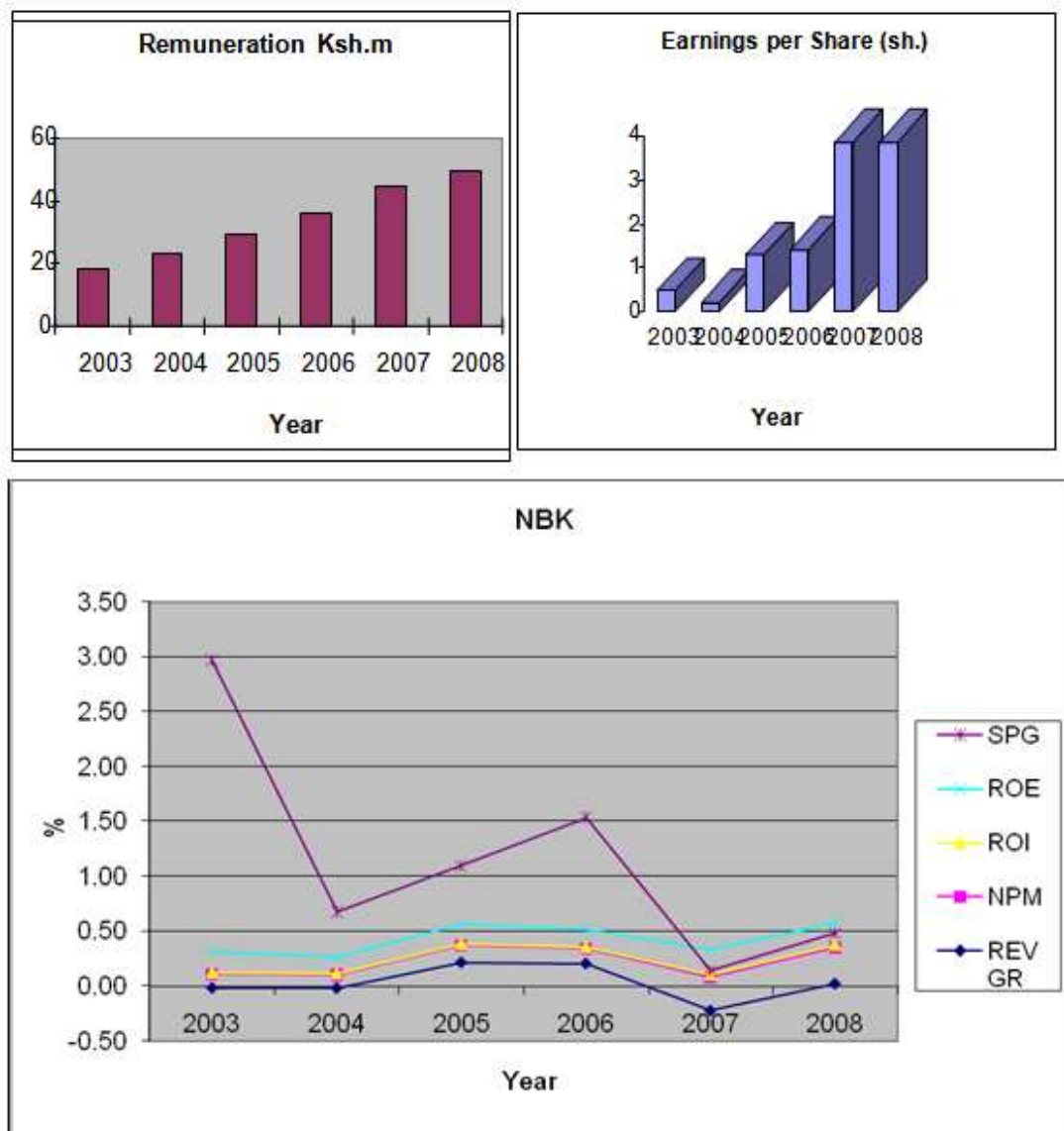
### Kenya Commercial Bank



**Figure 31 - Figure 4.29: Kenya Commercial Bank – Directors remuneration & performance measures**

The executive remuneration of Kenya Commercial Bank has been increasing steadily from 2003 to 2008. The number of directors was also the same over the period (11). The Earnings per Share of the bank increased and was very high in 2008 as compared to that of 2004 which was the lowest. The overall performance for the bank was good as shown by all the performance indicators. The share price however declined over the same period and was highly volatile. Additional factors that contributed to this performance was the banks expansion, reorganization to improve on operational efficiency, and increase in product lines.

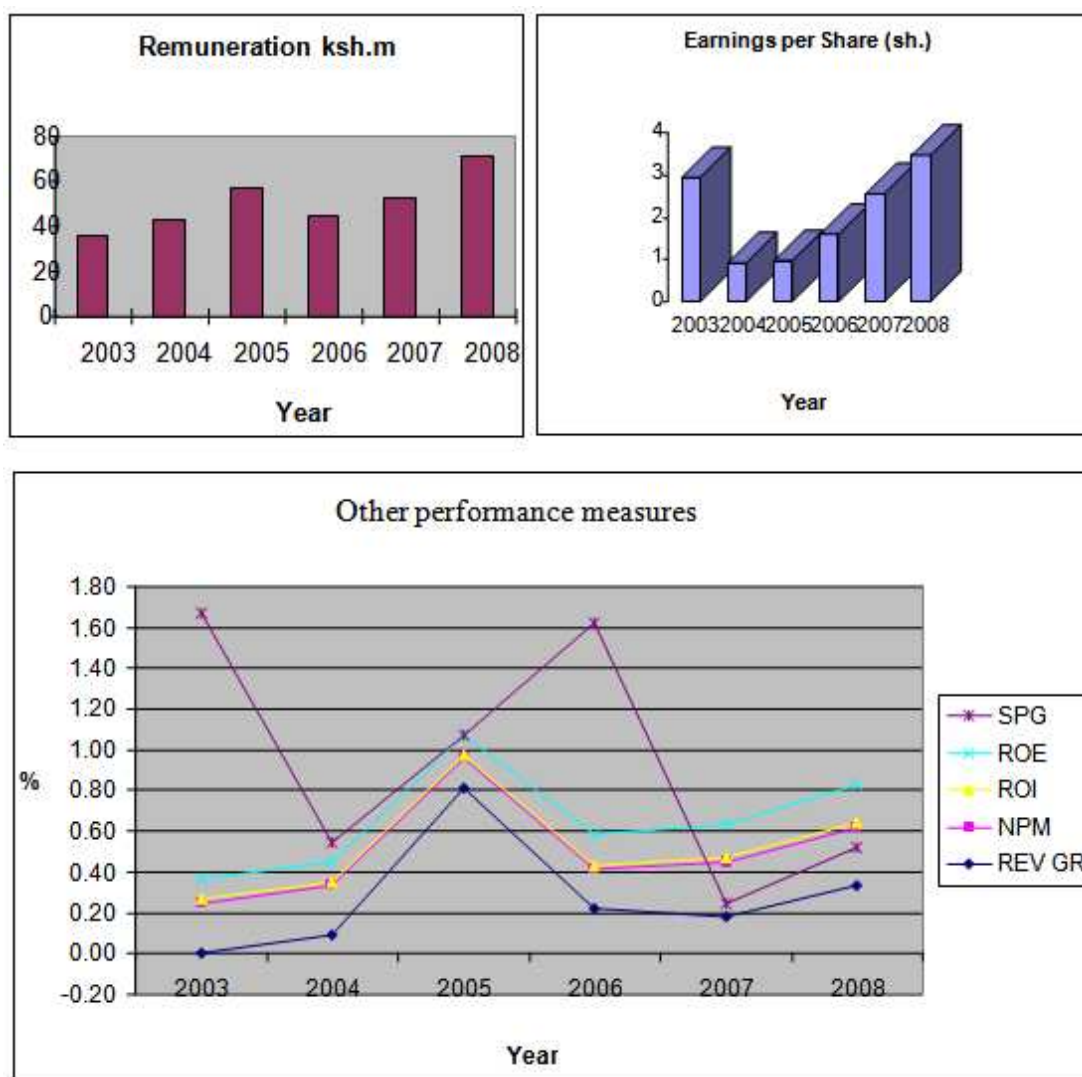
## National Bank



**Figure 32 - National Bank of Kenya – Directors remuneration & performance measures**

The remuneration of National Bank has increased steadily over the period under study as shown but the number of directors remained the same (12). The Earnings per Share has also increased with significant increases between 2005 and 2007. Apart from Share Price Growth, the other performance measures showed some improvement over the same period. National Bank embarked on a turnaround strategy that included debt recovery, cost control, investment in Information Technology Systems, and reassessment of its loan portfolio. These strategies enabled the bank to start making profits from 2003.

## National Industrial Credit

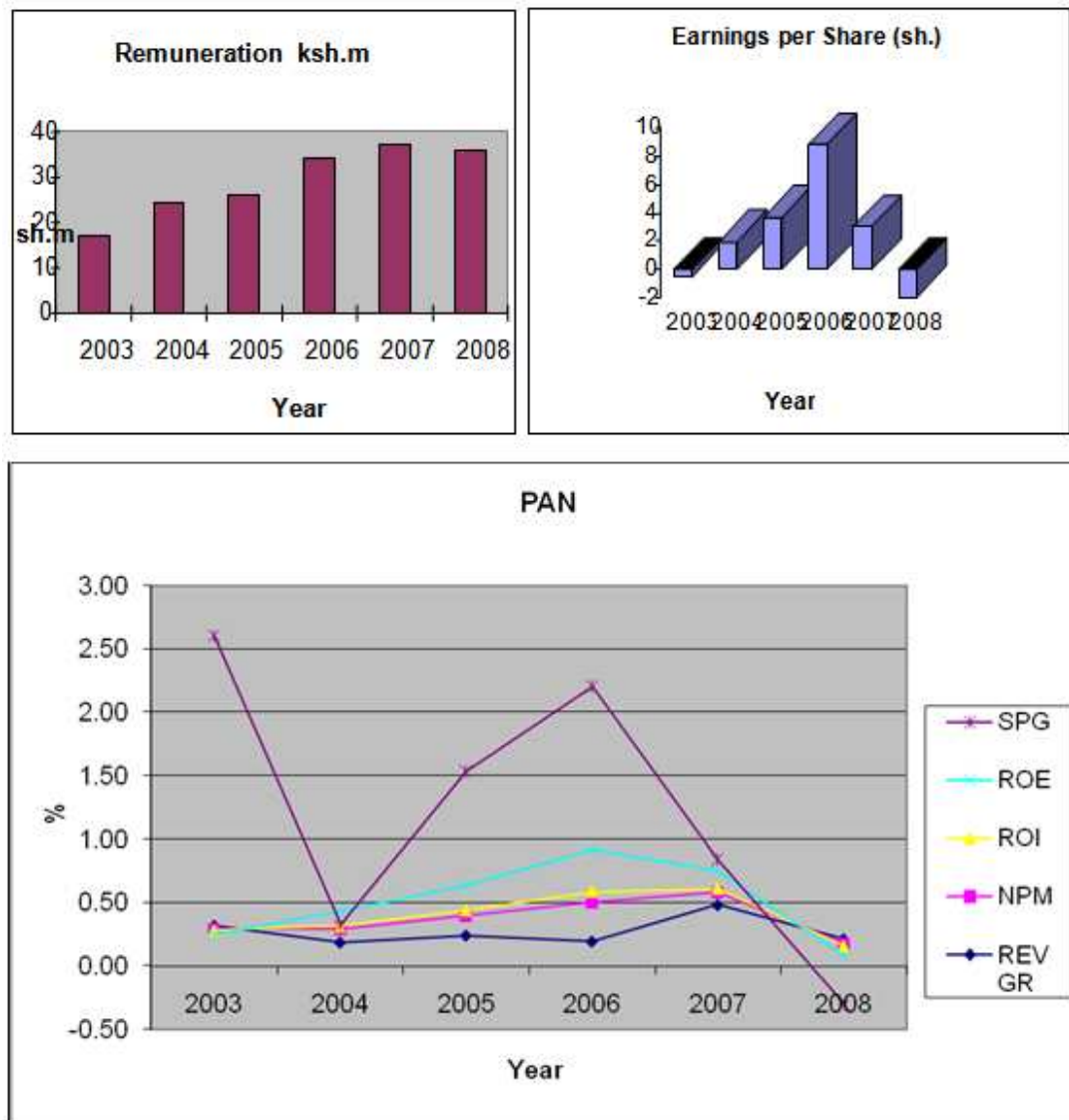


**Figure 33 - Figure 4.31: National Industrial Credit – Directors remuneration & performance measures**

The remuneration has been showing a steady increase over the period of study with the highest amount being paid in 2008. Initially the Earnings per Share declined up to 2004, but experienced a major increase from 2005 to 2008.

All the performance measures show some improvement over the period except for the share price. The bank undertook a major expansion to increase its market size. Overall profitability was largely attributed to a good economic environment especially for banks. In 2005 and 2006 there was reorganization that impacted adversely on the performance.

## Pan African Insurance



**Figure 34 - Figure 4.32: Pan Africa Insurance – Directors remuneration & performance measures**

Pan Africa Insurance reported a general increase in executive remuneration with a significant pay in 2007. The Earnings per Share showed a significant increase in 2006 but a major decline in year 2008. The other performance indicators have shown a similar pattern as that of earnings per share with the highest level reported in 2006 but a radical shift downwards. The company attributed the good performance in 2004 to 2006 to an increase in general insurance business as a result of more policies and

increase in insurance premium. From 2006, the decline in performance was attributed to expansion and high operational costs and poor investment returns.

### Standard Chartered Bank

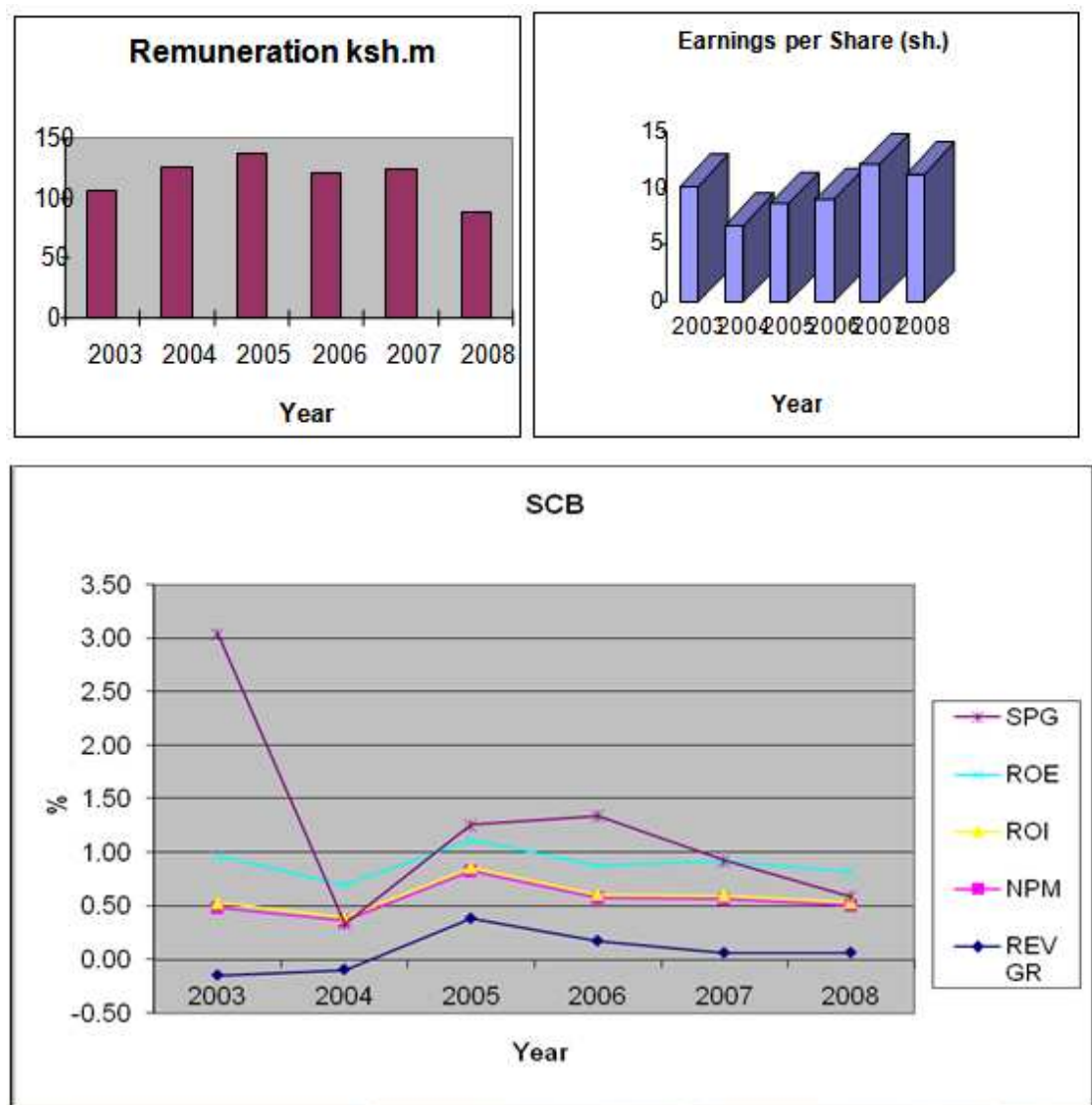


Figure 35 - Standard Chartered bank – Directors remuneration & performance measures

The Earnings per Share of Standard Chartered bank showed some stability but experienced a general decline in year 2008. The Earnings per Share showed some improvement from 2005 after reporting a slight decline. Other performance measures remained relatively stable over the period except for the share price which had some volatility. For all the banks considered, Standard Chartered Bank reported a decline in performance which the bank attributed to high operational costs and returns in investment income.

Table 13 provides a summary of the remuneration and performance indicators for each company in the sector:

**Table 13 - Summary Remuneration and Firm Performance – Finance & Investment**

|                            |     | REM    | REV GR  | NPM     | ROI    | ROE    | SPG      | EPS   |
|----------------------------|-----|--------|---------|---------|--------|--------|----------|-------|
|                            |     | Sh.m   | %       | %       | %      | %      | %        | Sh.   |
| Barclays Bank              | Max | 59     | 30.74%  | 47.29%  | 4.10%  | 31.09% | 177.23%  | 4.09  |
|                            | Min | 46     | 0.42%   | 31.82%  | 3.11%  | 27.00% | -70.72%  | 2.48  |
|                            | Avg | 51.67  | 14.88%  | 39.99%  | 3.69%  | 29.19% | 12.55%   | 3.16  |
| Centum Investment          | Max | 16.3   | 99.75%  | 150.62% | 13.24% | 13.36% | 2584.21% | 2.03  |
|                            | Min | 14.1   | -32.39% | 67.89%  | 5.44%  | 5.88%  | -73.12%  | 0.29  |
|                            | Avg | 15.13  | 35.26%  | 116.88% | 8.67%  | 9.02%  | 431.89%  | 1.00  |
| Diamond Trust Bank         | Max | 29.7   | 59.50%  | 45.23%  | 2.25%  | 17.86% | 180.00%  | 6.28  |
|                            | Min | 15.6   | 3.64%   | 24.43%  | 1.61%  | 10.41% | -28.04%  | 1.09  |
|                            | Avg | 20.87  | 29.49%  | 35.57%  | 1.83%  | 14.80% | 53.71%   | 3.13  |
| Housing Finance            | Max | 30.6   | 34.45%  | 10.31%  | 1.11%  | 7.36%  | 244.09%  | 0.88  |
|                            | Min | 25.2   | -43.35% | 2.55%   | 0.48%  | 3.72%  | -61.97%  | 0.45  |
|                            | Avg | 28.55  | -8.02%  | 6.86%   | 0.75%  | 5.17%  | 57.30%   | 0.63  |
| Jubilee Insurance          | Max | 34.1   | 117.23% | 16.07%  | 3.70%  | 22.25% | 289.16%  | 14.14 |
|                            | Min | 12.6   | 5.36%   | 11.14%  | 2.85%  | 11.98% | -42.25%  | 5.91  |
|                            | Avg | 28.02  | 38.19%  | 13.38%  | 3.34%  | 16.30% | 82.42%   | 10.31 |
| Kenya Commercial Bank      | Max | 113.7  | 57.32%  | 34.42%  | 2.63%  | 22.53% | 217.65%  | 1.97  |
|                            | Min | 57.4   | -7.19%  | 13.13%  | 0.91%  | 7.39%  | -88.17%  | 0.32  |
|                            | Avg | 84.3   | 22.98%  | 24.32%  | 1.81%  | 15.70% | 53.23%   | 1.01  |
| National Bank              | Max | 49.8   | 21.85%  | 32.79%  | 2.90%  | 22.53% | 265.75%  | 3.89  |
|                            | Min | 18.3   | -22.29% | 11.84%  | 1.25%  | 14.55% | -19.40%  | 0.21  |
|                            | Avg | 33.52  | 3.31%   | 19.27%  | 2.00%  | 18.44% | 71.94%   | 1.86  |
| National Industrial Credit | Max | 71.2   | 81.48%  | 27.70%  | 2.44%  | 18.65% | 130.96%  | 3.49  |
|                            | Min | 35.4   | -0.10%  | 14.23%  | 1.33%  | 9.43%  | -38.73%  | 0.90  |
|                            | Avg | 50.32  | 27.43%  | 22.86%  | 1.95%  | 13.11% | 29.29%   | 2.07  |
| Pan Africa Insurance       | Max | 37.5   | 48.17%  | 30.42%  | 9.07%  | 32.62% | 235.71%  | 8.87  |
|                            | Min | 17.1   | 18.66%  | -3.82%  | -1.58% | -8.09% | -37.69%  | -1.99 |
|                            | Avg | 29.2   | 27.30%  | 9.72%   | 2.98%  | 10.87% | 69.23%   | 2.51  |
| Standard Chartered Bank    | Max | 136.4  | 38.69%  | 63.03%  | 4.35%  | 43.31% | 208.06%  | 12.14 |
|                            | Min | 87.4   | -14.43% | 40.18%  | 2.73%  | 25.57% | -36.13%  | 6.74  |
|                            | Avg | 116.72 | 7.64%   | 47.70%  | 3.47%  | 30.86% | 35.09%   | 9.71  |

The table shows that Standard Chartered bank paid the highest remuneration to its directors followed by Kenya Commercial Bank. However Centum investment showed a significantly better performance than other companies in the sector.

Table 14 summarises the average performance of the sector over the six years:

**Table 14 - Annual remuneration and firm performance for Finance and Investment sector**

|           | 2003   | 2004   | 2005   | 2006    | 2007   | 2008   | Average |
|-----------|--------|--------|--------|---------|--------|--------|---------|
| REM sh. m | 36.96  | 41.7   | 47.4   | 47.7    | 51.26  | 49.95  | 45.83   |
| REV GR-%  | 15.28% | 6.12%  | 21.78% | 23.26%  | 29.06% | 23.57% | 20%     |
| NPM -%    | 26.23% | 26.45% | 32.98% | 40.24%  | 38.59% | 37.44% | 34%     |
| ROI -%    | 2.26%  | 2.59%  | 2.88%  | 3.87%   | 3.74%  | 2.95%  | 3%      |
| ROE -%    | 14.18% | 14.39% | 15.98% | 19.18%  | 18.38% | 15.97% | 16%     |
| SPG -%    | 435.9% | 1.26%  | 38.62% | 113.22% | -21.6% | -28.9% | 90%     |
| EPS -sh.  | 2.378  | 2.18   | 3.075  | 4.255   | 4.785  | 4.558  | 3.54    |

Table 14 shows that the average remuneration for the entire sector has been increasing as in the case of the other sectors. So far this sector has reported the highest average remuneration as compared to the other sectors.

In terms of performance the finance and investment sector also reported as steady increase in the general measures of performance except that of share price which declined sharply in 2007.

Table 15 provides a summary of the regression results for each company in the sector.

**Table 15 - Summary regression results for companies -Finance & Investment**

|                        |             | Remuneration Vs |         |         |         |         |           |
|------------------------|-------------|-----------------|---------|---------|---------|---------|-----------|
|                        |             | REV GR (%)      | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
| Barclays Bank of Kenya | $\alpha$    | 47.7            | 77.8    | 63.9    | 125     | 52      | 35.4      |
|                        | $P(\alpha)$ | 0.000           | 0.004   | 0.049   | 0.009   | 0.000   | 0.027     |
|                        | $\beta$     | 0.2634          | -0.6536 | -3.317  | -2.4974 | -0.0267 | 5.141     |
|                        | $P(\beta)$  | 0.173           | 0.12    | 0.618   | 0.05    | 0.357   | 0.189     |
|                        | $R^2$       | 40.70%          | 49.20%  | 6.80%   | 65.80%  | 21.30%  | 38.40%    |
|                        | DW          | 2.03            | 1.8     | 1.8     | 2.05    | 2.3     | 2.04      |
| Centum Investment      | $\alpha$    | 15              | 15.3    | 14.3    | 14.3    | 15.1    | 14.7      |
|                        | $P(\alpha)$ | 0.00            | 0.000   | 0.00    | 0.000   | 0.000   | 0.000     |
|                        | $\beta$     | 0.003578        | -0.0022 | 0.0924  | 0.0965  | 6.2E-06 | 0.4136    |
|                        | $P(\beta)$  | 0.598           | 0.825   | 0.435   | 0.441   | 0.986   | 0.417     |
|                        | $R^2$       | 7.60%           | 1.40%   | 15.80%  | 15.50%  | 0.00%   | 17.00%    |
|                        | DW          | 2.1             | 2.1     | 2       | 1.8     | 2.01    | 2         |

|                            |             |         |        |         |         |         |         |
|----------------------------|-------------|---------|--------|---------|---------|---------|---------|
| Diamond Trust Bank         | $\alpha$    | 15.2    | 10.7   | 15.6    | 12.5    | 23.1    | 13.9    |
| Housing Finance            | $P(\alpha)$ | 0.007   | 0.317  | 0.477   | 0.359   | 0.00    | 0.003   |
|                            | $\beta$     | 0.19237 | 0.2849 | 2.86    | 0.5656  | -0.0423 | 2.2058  |
|                            | $P(\beta)$  | 0.091   | 0.331  | 0.804   | 0.519   | 0.153   | 0.02    |
|                            | $R^2$       | 55.20%  | 23.40% | 1.70%   | 11.10%  | 43.70%  | 78.00%  |
|                            | DW          | 1.6     | 1.38   | 0.91    | 1.1     | 1.18    | 2.3     |
|                            | $\alpha$    | 28.6    | 27.7   | 27.2    | 30.4    | 28.8    | 27.8    |
|                            | $P(\alpha)$ | 0.00    | 0.000  | 0.001   | 0.002   | 0.00    | 0.002   |
|                            | $\beta$     | 0.00569 | 1.783  | -0.3527 | -0.0047 | 1.166   | 0       |
|                            | $P(\beta)$  | 0.891   | 0.694  | 0.693   | 0.608   | 0.854   | 0       |
|                            | $R^2$       | 0.50%   | 4.30%  | 4.30%   | 7.20%   | 1.00%   | 0.00%   |
| Jubilee Insurance          | DW          | 2.04    | 2.02   | 2.01    | 2.06    | 2.06    | 2.3     |
|                            | $\alpha$    | 28.6    | 15.4   | 47.34   | 55.8    | 25.3    | 42      |
|                            | $P(\alpha)$ | 0.006   | 0.587  | 0.247   | 0.001   | 0.002   | 0.014   |
|                            | $\beta$     | -0.0164 | 0.941  | -5.79   | -1.7051 | 0.03274 | -1.3611 |
|                            | $P(\beta)$  | 0.878   | 0.653  | 0.608   | 0.084   | 0.246   | 0.222   |
|                            | $R^2$       | 0.70%   | 5.60%  | 7.20%   | 56.60%  | 31.60%  | 34.30%  |
|                            | DW          | 0.73    | 0.54   | 0.97    | 1.04    | 1.39    | 1.13    |
|                            | $\alpha$    | 65.6    | 24.5   | 31.08   | 25.7    | 92.5    | 48.8    |
|                            | $P(\alpha)$ | 0.02    | 0.211  | 0.08    | 0.054   | 0.001   | 0.002   |
|                            | $\beta$     | 0.8112  | 2.4594 | 29.459  | 3.7325  | -0.154  | 35.158  |
| Kenya Commercial Bank      | $P(\beta)$  | 0.044   | 0.019  | 0.013   | 0.003   | 0.14    | 0.004   |
|                            | $R^2$       | 67.80%  | 78.50% | 82.00%  | 91.50%  | 45.80%  | 90.40%  |
|                            | DW          | 1.9     | 1.39   | 1.46    | 1.8     | 1.49    | 2.3     |
|                            | $\alpha$    | 33.9    | 11.6   | -0.77   | -13.6   | 39.8    | 20.29   |
|                            | $P(\alpha)$ | 0.004   | 0.132  | 0.925   | 0.702   | 0.001   | 0.002   |
|                            | $\beta$     | -0.1461 | 1.1398 | 17.176  | 2.556   | -0.0878 | 7.103   |
|                            | $P(\beta)$  | 0.71    | 0.017  | 0.01    | 0.224   | 0.087   | 0.004   |
|                            | $R^2$       | 3.80%   | 79.60% | 84.30%  | 34.00%  | 55.90%  | 89.70%  |
|                            | DW          | 0.34    | 1.58   | 2.1     | 1.2     | 1.35    | 2.37    |
|                            | $\alpha$    | 43.5    | 44.28  | 36.3    | 21.2    | 54.1    | 42.3    |
| National Industrial Credit | $P(\alpha)$ | 0.003   | 0.197  | 0.241   | 0.255   | 0.000   | 0.028   |
|                            | $\beta$     | 0.2479  | 0.264  | 7.17    | 2.222   | -0.1324 | 3.865   |
|                            | $P(\beta)$  | 0.24    | 0.84   | 0.617   | 0.131   | 0.089   | 0.519   |
|                            | $R^2$       | 32.20%  | 1.10%  | 6.80%   | 47.30%  | 55.60%  | 11.10%  |
|                            | DW          | 0.66    | 1.14   | 1.3     | 2.05    | 2.08    | 1.2     |
|                            | $\alpha$    | 25.4    | 27.4   | 27.5    | 27.7    | 32.6    | 27.7    |
|                            | $P(\alpha)$ | 0.067   | 0.004  | 0.0004  | 0.004   | 0.001   | 0.003   |
|                            | $\beta$     | 0.1384  | 0.188  | 0.5856  | 0.1408  | -0.0489 | 0.591   |
|                            | $P(\beta)$  | 0.712   | 0.57   | 0.586   | 0.616   | 0.183   | 0.593   |
|                            | $R^2$       | 3.80%   | 8.70%  | 8.00%   | 6.90%   | 39.30%  | 7.70%   |
| Pan Africa Insurance       | DW          | 0.54    | 0.34   | 0.34    | 0.33    | 1       | 0.35    |
|                            | $\alpha$    | 113.5   | 138.7  | 139.8   | 142.56  | 117.8   | 159     |
|                            | $P(\alpha)$ | 0.000   | 0.051  | 0.059   | 0.022   | 0.000   | 0.014   |
|                            | $\beta$     | 0.4192  | -0.463 | -6.66   | -0.837  | -0.0327 | -4.314  |
|                            | $P(\beta)$  |         |        |         |         |         |         |
|                            | $R^2$       |         |        |         |         |         |         |
|                            | DW          |         |        |         |         |         |         |
|                            | $\alpha$    |         |        |         |         |         |         |
|                            | $P(\alpha)$ |         |        |         |         |         |         |
|                            | $\beta$     |         |        |         |         |         |         |
| Standard Chartered Bank    | $P(\beta)$  |         |        |         |         |         |         |
|                            | $R^2$       |         |        |         |         |         |         |
|                            | DW          |         |        |         |         |         |         |
|                            | $\alpha$    |         |        |         |         |         |         |
|                            | $P(\alpha)$ |         |        |         |         |         |         |
|                            | $\beta$     |         |        |         |         |         |         |
|                            | $P(\beta)$  |         |        |         |         |         |         |
|                            | $R^2$       |         |        |         |         |         |         |
|                            | DW          |         |        |         |         |         |         |
|                            | $\alpha$    |         |        |         |         |         |         |

|                |        |       |       |        |       |        |
|----------------|--------|-------|-------|--------|-------|--------|
| P( $\beta$ )   | 0.354  | 0.68  | 0.685 | 0.541  | 0.75  | 0.328  |
| R <sup>2</sup> | 21.50% | 4.70% | 4.50% | 10.00% | 2.80% | 23.70% |
| DW             | 1.52   | 1.48  | 1.5   | 1.45   | 1.29  | 2.1    |

Kenya Commercial Bank is the only bank in the Finance and Investments sector that has reported a significant positive relationship between executive remuneration and firm performance (except for share price growth which is significantly negative). All the others have reported mixed relationships which are not significant. Therefore, apart from Kenya Commercial Bank, we fail to reject the Null hypothesis and conclude that for companies in the finance and investment sector, there is no evidence of a significant positive relationship between executive remuneration and firm performance.

Table 16 also provides summarised regression results for the Finance and Investment industry are given as follows:

**Table 16 - Summary regression – Finance and Investments**

| Remuneration Vs |            |         |         |         |         |           |
|-----------------|------------|---------|---------|---------|---------|-----------|
|                 | REV GR (%) | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
| $\alpha$        | 46.8       | 46.8    | 49.9    | 14.59   | 47.2    | 35.8      |
| P( $\alpha$ )   | 0.000      | 0.000   | 0.000   | 0.04    | 0.000   | 0.000     |
| $\beta$         | -0.05      | -0.02   | -1.33   | 1.9     | -0.015  | 2.84      |
| P( $\beta$ )    | 0.727      | 0.817   | 0.422   | 0.000   | 0.212   | 0.009     |
| R <sup>2</sup>  | 0.2%       | 0.1%    | 1.1%    | 32%     | 2.7%    | 11.2%     |
| DW <sup>9</sup> | 1.85       | 1.9     | 1.78    | 1.9     | 1.7     | 1.75      |

Most of the performance indicators show a negative relationship with remuneration except that of Return on Equity. The alpha ( $\alpha$ ) appears to be significant but the beta relations are not significant. For the entire finance and investment sector we also fail to reject the null hypothesis and conclude that there is no evidence of a significant positive relationship between executive remuneration and firm performance.

<sup>9</sup> For the sector analysis the where n=60 and k=1 the DW factors lie between 1.54 and 1.61 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

#### 4.2.5 Alternative Investments

The general trend in this sector showed a decline in performance levels. The remuneration also in the sector showed a general decline especially that of Williamson. This is summarised from figures 36 to 38. The regression results summarised in tables 17 and 20 did not show any evidence of relationship between remuneration and firm performance measures.

#### Express Kenya Limited

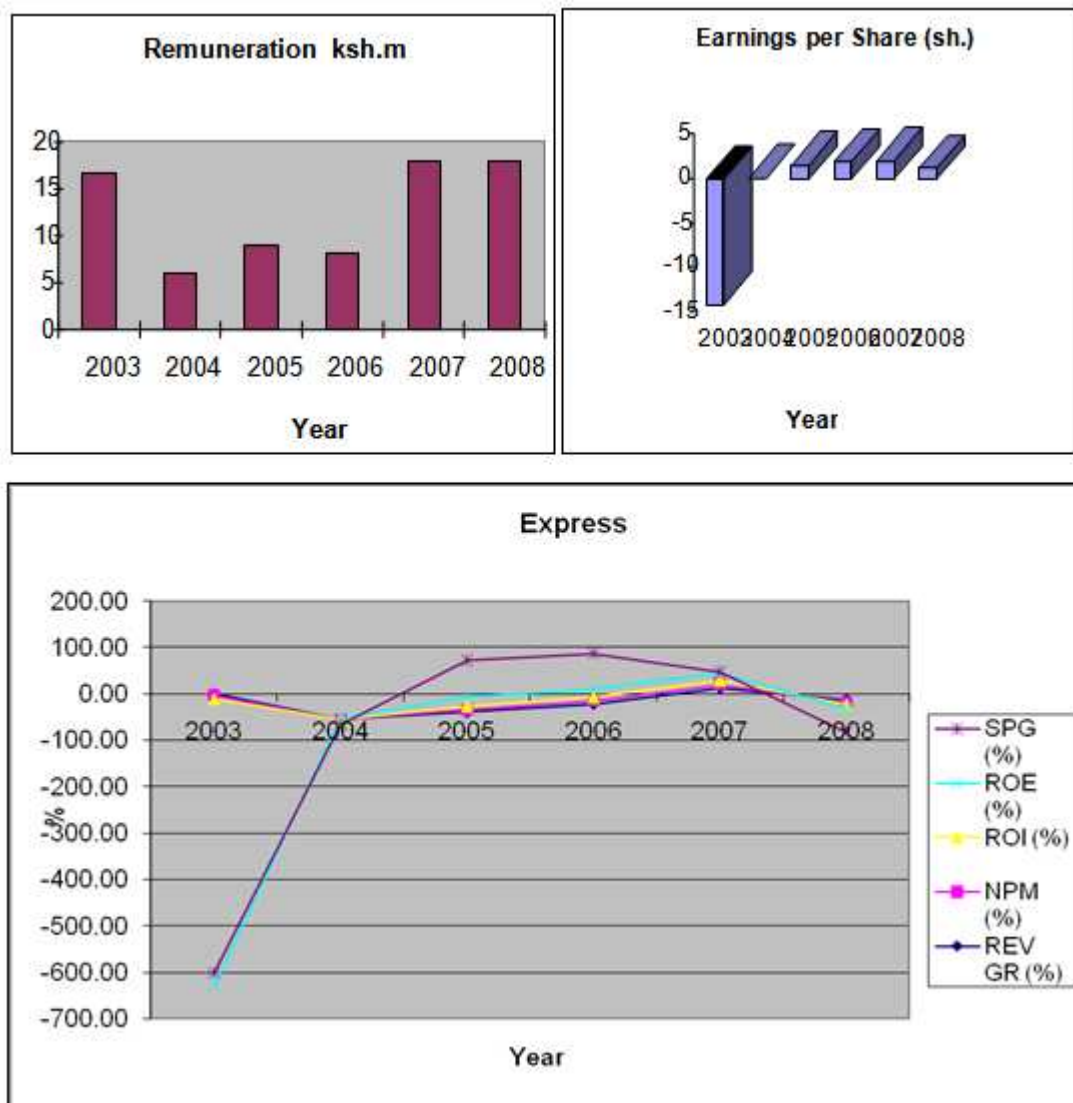


Figure 36 - Express Kenya – Directors remuneration & performance measures

The remuneration for Express Kenya was stable between 2003 and 2008 but the company paid reduced amounts in 2004, 2005 and 2006. The number of directors still

remained the same over the period. The company reported an improvement in Earnings per share in 2004, which remained relatively the same from 2005 to 2008. The other performance measures improved also in 2004 up to 2005 and 2006 when the performance declined from 2007 and 2008. The initial improvement in performance in 2004 to 2006 was due to reduction in finance costs and savings in other operational costs. The period from 2006 to 2007 reported a decline in the performance due to poor infrastructure, high operating expenses and in 2008, the post election violence meant that business was slow and transport was hampered.

### Kapchorua Tea

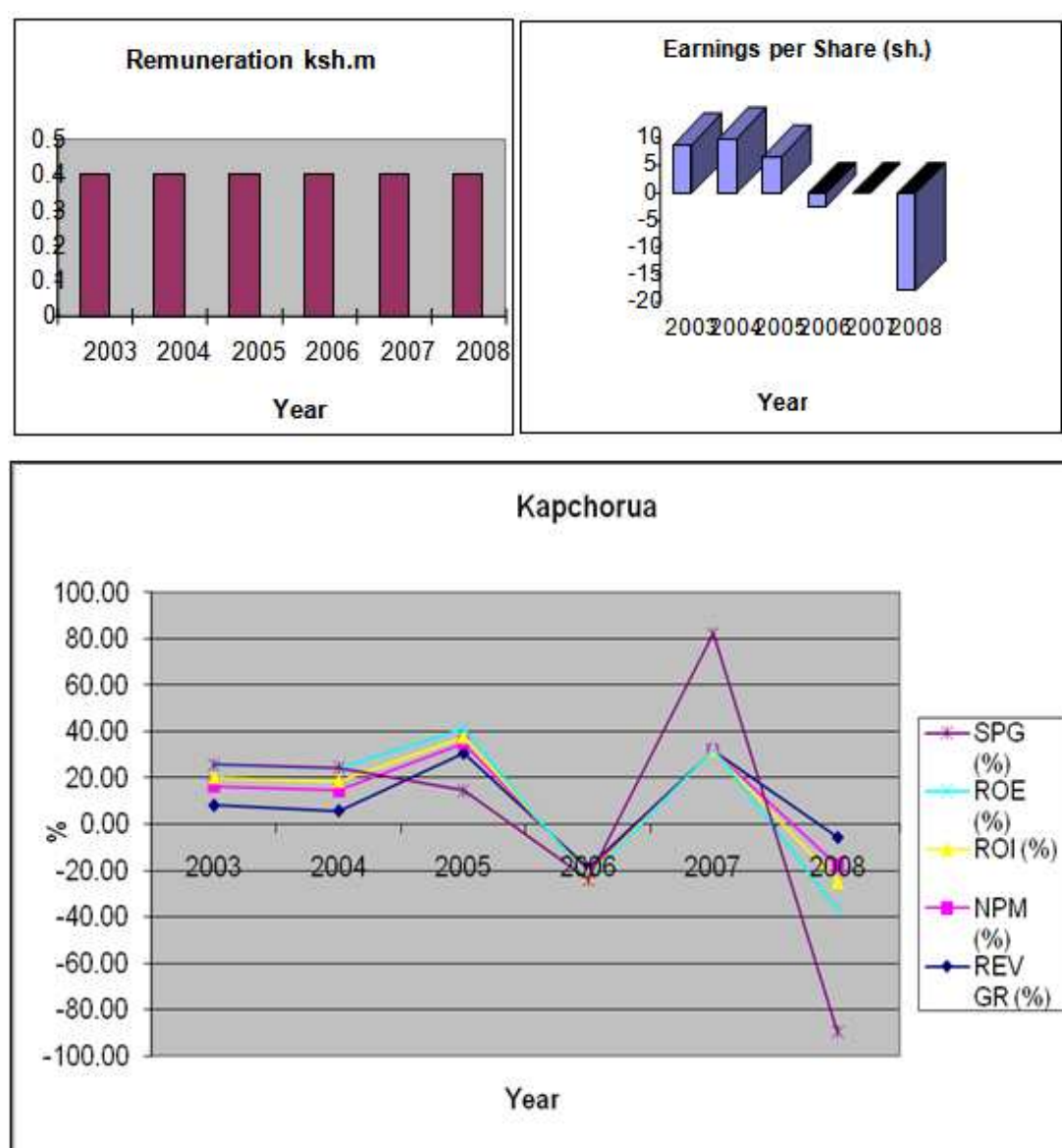
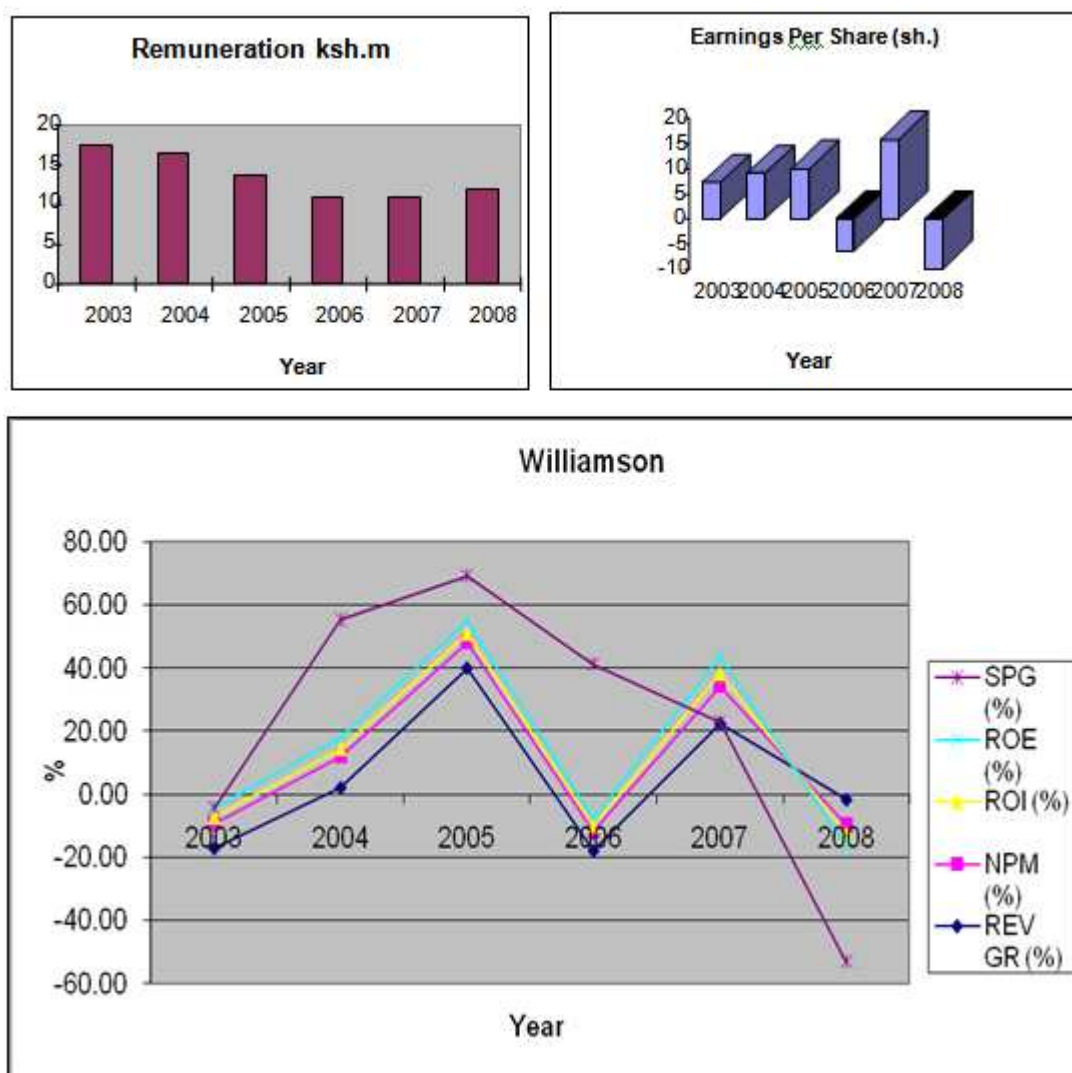


Figure 37 - Kapchorua Tea – Directors remuneration & performance measures

Kapchorua was the only company that reported constant directors' remuneration which implies that there is no relationship with firm performance. Consequently, there was no regression for Kapchorua Tea. The number of directors also remained the same. The Earnings per Share for Kapchorua declined over the years with significant negative Earnings per Share in 2008.

The same trend is reported in the other performance measures which had improved in 2005 but declined significantly in 2006. There was some further improvement in 2007 followed by another significant decline in 2008. The share price tends to behave in a similar manner. The decline in performance was largely blamed on poor weather conditions, lower tea prices in the world markets and adverse foreign exchange rates. The company however, embarked on investment and improving the manufacturing processes.

## Williamson Tea



**Figure 38 - Williamson Tea – Directors remuneration & performance measures**

The executive remuneration for Williamson showed a general decline over the years but not very significant. The number of directors remained constant. The Earnings per Share has shown a mixed trend but a general decline as at the end of 2008. The volatility in the company's performance was also blamed to inconsistent weather patterns, varying crop productions, reduced world tea prices, decline in market value of biological assets and post election violence in 2008.

Table 17 provides a summary of remuneration and the performance indicators for each company in the sector.

**Table 17 - Summary Remuneration and Firm Performance – Alternative investments**

|                |     | REM   | REV GR  | NPM     | ROI    | ROE     | SPG     | EPS   |
|----------------|-----|-------|---------|---------|--------|---------|---------|-------|
|                |     | Sh.m  | %       | %       | %      | %       | %       | Sh.   |
| Express Kenya  | Max | 18    | 12.17%  | 8.03%   | 8.98%  | 21.34%  | 76.92%  | 2.08  |
|                | Min | 6     | -55.56% | -5.35%  | -8.38% | -618.2% | -50.61% | -14.2 |
|                | Avg | 12.63 | -19.84% | 2.40%   | 2.38%  | -95.03% | 19.72%  | -1.23 |
| Kapchorua Tea  | Max | 0.4   | 31.75%  | 8.90%   | 3.93%  | 5.79%   | 50.00%  | 9.88  |
|                | Min | 0.4   | -19.06% | -12.17% | -7.13% | -11.27% | -53.33% | -17.8 |
|                | Avg | 0.4   | 8.57%   | 1.29%   | 0.34%  | 0.39%   | -5.06%  | 0.81  |
| Williamson Tea | Max | 17.4  | 39.95%  | 11.86%  | 3.81%  | 5.55%   | 48.75%  | 15.96 |
|                | Min | 10.8  | -17.78% | -8.18%  | -2.71% | -3.97%  | -36.51% | -9.91 |
|                | Avg | 13.58 | 4.68%   | 5.84%   | 1.73%  | 2.47%   | 7.20%   | 4.40  |

Generally alternative investment was the worst performing sector in terms of paying directors and also other performance indicators. Williamson tea reported the highest remuneration and was also better in terms of performance as compared to the others.

Table 18 provides a summary of remuneration and average performance for the entire sector.

**Table 18 - Annual remuneration and firm performance for Alternative Investments**

|             | 2003   | 2004   | 2005   | 2006    | 2007   | 2008    | Average |
|-------------|--------|--------|--------|---------|--------|---------|---------|
| REM (sh. m) | 11.53  | 7.67   | 7.73   | 6.43    | 9.73   | 10.13   | 8.87    |
| REV GR (%)  | -3.15% | -15.9% | 10.14% | -19.64% | 22.12% | -6.77%  | -2%     |
| NPM (%)     | 4.83%  | 6.29%  | 5.89%  | 3.92%   | 6.68%  | -8.57%  | 3%      |
| ROI (%)     | -0.90% | 2.44%  | 4.72%  | 2.72%   | 4.29%  | -4.37%  | 1%      |
| ROE (%)     | -203%  | 3.98%  | 9.75%  | 6.18%   | 7.45%  | -8.40%  | -31%    |
| SPG (%)     | 9.52%  | 7.97%  | 21.40% | 41.49%  | 10.15% | -46.82% | 7%      |
| EPS (sh.)   | 0.69   | 6.40   | 6.09   | -2.31   | 5.93   | -8.84   | 1.33    |

As indicated before the sector has not performed well and this is highlighted by the general decline in remuneration. All the performance indicators have also been

declining. Table 19 provides a summary of the regression result for each company apart from Kapchorua Tea.

**Table 19 - Individual companies regression results - Alternative Investment**

|                      |                | Remuneration Vs |         |         |          |         |           |
|----------------------|----------------|-----------------|---------|---------|----------|---------|-----------|
|                      |                | REV GR (%)      | NPM (%) | ROI (%) | ROE (%)  | SPG (%) | EPS (sh.) |
| Express Kenya        | $\alpha$       | 16.5            | 13.4    | 13.3    | 11.89    | 13.7    | 12.29     |
|                      | P( $\alpha$ )  | 0.00            | 0.007   | 0.006   | 0.009    | 0.005   | 0.007     |
|                      | $\beta$        | 0.19453         | -0.3312 | -0.2918 | -        | -       | -0.2763   |
|                      |                |                 |         |         | 0.008249 | 0.05351 |           |
|                      | P( $\beta$ )   | 0.021           | 0.523   | 0.459   | 0.455    | 0.324   | 0.538     |
|                      | R <sup>2</sup> | 77.30%          | 10.90%  | 14.40%  | 14.60%   | 24.00%  | 10.20%    |
|                      | DW             | 1.58            | 1.77    | 1.66    | 1.09     | 2.06    | 1.16      |
| Williamson Tea Kenya | $\alpha$       | 13.7            | 13      | 13.3    | 13.27    | 13.5    | 13.19     |
|                      | P( $\alpha$ )  | 0.000           | 0.002   | 0.001   | 0.001    | 0.001   | 0.001     |
|                      | $\beta$        | -0.02401        | 0.0966  | 0.1852  | 0.1243   | 0.01843 | 0.0894    |
|                      | P              | 0.718           | 0.645   | 0.78    | 0.785    | 0.688   | 0.541     |
|                      | R <sup>2</sup> | 3.60%           | 5.80%   | 2.20%   | 2.10%    | 4.50%   | 10.00%    |
|                      | DW             | 0.6             | 0.65    | 0.55    | 0.55     | 0.609   | 0.75      |

Again based on the P value, we fail to reject the Null hypothesis and conclude that there is no evidence of a significant positive relationship between executive remuneration and firm performance. Table 20 provides the summary regression for the entire sector.

**Table 20 - Summary regression results – Alternative Investments**

|                |  | Remuneration Vs |         |         |         |         |           |
|----------------|--|-----------------|---------|---------|---------|---------|-----------|
|                |  | REV GR (%)      | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
| $\alpha$       |  | 8.8             | 8.36    | 8.81    | 8.47    | 8.78    | 8.8       |
| P( $\alpha$ )  |  | 0.000           | 0.00    | 0.00    | 0.00    | 0.00    | 0.00      |
| $\beta$        |  | -0.019          | 0.16    | 0.039   | -0.013  | 0.0121  | 0.033     |
| P( $\beta$ )   |  | 0.789           | 0.538   | 0.918   | 0.273   | 0.79    | 0.868     |
| R <sup>2</sup> |  | .05%            | 2.5%    | 0.01%   | 7.5%    | 0.5%    | 0.2%      |
| DW             |  | 2.18            | 2.08    | 2.29    | 2.1     | 2.18    | 2.08      |

Performance indicators show mixed relations with a revenue growth, and return on equity showing a negative relationship and Net profit margin, Return on Investment, share price growth and earnings per share showing a positive relationship. These relationships are not significant as indicated by the various betas and therefore we fail

to reject the Null hypothesis. There is no evidence of a strong positive relationship between executive remuneration and firm performance.

#### 4.2.6 Analysis for all the companies

Table 21 provides a summary of the key performance indicators for the entire market:

**Table 21 - Remuneration and firm performance for the entire stock Market**

|             | 2003    | 2004   | 2005   | 2006   | 2007   | 2008   | Average |
|-------------|---------|--------|--------|--------|--------|--------|---------|
| REM (sh. m) | 30.31   | 33.87  | 38.88  | 41.30  | 43.85  | 45.82  | 39.00   |
| REV GR (%)  | 8.51%   | 17.41% | 20.50% | 14.95% | 21.64% | 17.16% | 16.70%  |
| NPM (%)     | 9.92%   | 15.09% | 14.13% | 17.38% | 17.04% | 16.43% | 15.00%  |
| ROI (%)     | 3.32%   | 7.26%  | 7.20%  | 7.01%  | 7.52%  | 6.42%  | 6.45%   |
| ROE (%)     | -14.29% | 15.46% | 15.90% | 16.44% | 17.30% | 13.48% | 10.72%  |
| SPG (%)     | 236.74% | 34.49% | 48.13% | 63.71% | -      | -      | 58.08%  |
|             |         |        |        |        | 13.12% | 21.44% |         |
| EPS (sh.)   | 1.09    | 3.74   | 4.05   | 4.38   | 5.71   | 4.32   | 3.88    |

Generally the average remuneration for the entire NSE increased but most of the performance indicators like net Profit Margin and Return on Equity and Earnings Per Share were stable. Only the share price growth was negative.

Table 22 provides a regression analysis for all the companies over the six years.

**Table 22 - Summary regression results – All the companies**

| Remuneration Vs  |            |         |         |         |         |           |
|------------------|------------|---------|---------|---------|---------|-----------|
|                  | REV GR (%) | NPM (%) | ROI (%) | ROE (%) | SPG (%) | EPS (sh.) |
| $\alpha$         | 38.8       | 34.2    | 23.05   | 37.4    | 39      | 32.7      |
| $P(\alpha)$      | 0.000      | 0.000   | 0.000   | 0.000   | 0.00    | 0.000     |
| $\beta$          | 0.015      | 0.317   | 2.4     | 0.14    | -0.015  | 1.6       |
| $P(\beta)$       | 0.89       | 0.06    | 0.01    | 0.06    | 0.25    | 0.02      |
| $R^2$            | 0.0%       | 3.4%    | 18.7%   | 2.4%    | 0.6%    | 0.2%      |
| DW <sup>10</sup> | 2.02       | 2.01    | 2.11    | 2.11    | 2.1     | 2.01      |

All the performance indicators show a positive relationship between firm performance and remuneration except that of share price growth which shows a negative relationship. The results also indicate that Return on Investment and Earnings Per share are significant. Except for these two performance indicators we also fail to

<sup>10</sup> For the total analysis the where  $n > 200$  and  $k = 1$  the DW factors lie between 1.71 and 1.72 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

reject the Null hypothesis and conclude that there is no evidence of a strong positive relationship between executive remuneration and firm performance.

An additional analysis was carried to check relationship between Remuneration and firm size as measured by Revenue, Total Assets and Total Equity. Table 23 summarises the results.

**Table 23 - Remuneration, Revenue, Total Assets and Total equity**

|                        | <b>Remuneration</b> | <b>Revenue</b> | <b>Total Assets</b> | <b>Total Equity</b> |
|------------------------|---------------------|----------------|---------------------|---------------------|
| Maximum (sh.m)         | 216                 | 60,417         | 191,211             | 25,164              |
| Minimum (sh.m)         | 0.4                 | 139            | 356                 | 5.8                 |
| Average (sh.m)         | 39                  | 6,908          | 16,882.7            | 43.94               |
| <b>Remuneration Vs</b> |                     | <b>Revenue</b> | <b>Total Assets</b> | <b>Total Equity</b> |
| $\alpha$               |                     | 27.4           | 28.4                | 18.7                |
| P( $\alpha$ )          |                     | 0.00           | 0.00                | 0.00                |
| $\beta$                |                     | 0.0015         | 0.0005              | 0.004               |
| P( $\beta$ )           |                     | 0.00           | 0.00                | 0.00                |
| R <sup>2</sup>         |                     | 17.5%          | 19.3%               | 38.1%               |
| DW <sup>11</sup>       |                     | 0.8            | 1.2                 | 1.4                 |

The table shows that the highest total revenue to be paid in a financial period was sh. 216 million that was paid by East African Breweries while the average was sh. 39 million. The lowest remuneration paid to directors was sh.0.4 million by Kapchorua tea.

The regression results also show that there is a significant positive relationship between executive remuneration and firm size as measured by all the indicators although Equity appears to be the significant one. Therefore it appears there is positive relationship between remuneration and firm size. The results for revenue however appear not be conclusive because of the very significantly lower Durbin Watson.

Table 24 also provides additional summaries by sectors and also for the entire market. Table 24 summarises average remuneration paid to directors by sector and also for the entire stock market

<sup>11</sup> For the total analysis the where  $n > 200$  and  $k = 1$  the DW factors lie between 1.71 and 1.72 at 95% confidence level, see [www.nd.edu/~wevans1/econ30331/Durbin\\_Watson\\_tables.pdf](http://www.nd.edu/~wevans1/econ30331/Durbin_Watson_tables.pdf)

**Table 24 - Average Remuneration by sector (sh.m)**

|                         | 2003  | 2004  | 2005  | 2006  | 2007  | 2008  | Average |
|-------------------------|-------|-------|-------|-------|-------|-------|---------|
| Agriculture             | 9.37  | 14.30 | 14.63 | 12.37 | 17.37 | 14.67 | 13.78   |
| Commercial & Services   | 42.54 | 36.69 | 43.73 | 45.86 | 51.29 | 45.63 | 44.29   |
| Industrial & Allied     | 27.95 | 36.68 | 42.25 | 48.11 | 47.82 | 57.29 | 43.35   |
| Finance & investment    | 36.96 | 41.7  | 47.4  | 47.7  | 51.26 | 49.95 | 45.83   |
| Alternative investments | 11.53 | 7.67  | 7.73  | 6.43  | 9.73  | 10.13 | 8.87    |
| Nairobi Stock Exchange  | 30.31 | 33.87 | 38.88 | 41.30 | 43.85 | 45.82 | 39.00   |

Table 25 provides a summary of Revenue growth for each sector and also for the total.

**Table 25 - Average Revenue Growth by sector**

|                         | 2003   | 2004   | 2005   | 2006   | 2007   | 2008   | Average |
|-------------------------|--------|--------|--------|--------|--------|--------|---------|
| Agriculture             | 10%    | 17%    | -2%    | 23%    | 6%     | 9%     | 10%     |
| Commercial & Services   | 2.61%  | 16.60% | 32.51% | 17.54% | 14.63% | 9.43%  | 16%     |
| Industrial & Allied     | 8.76%  | 33.08% | 20.62% | 13.40% | 23.19% | 23.32% | 20%     |
| Finance & Investment    | 15.28% | 6.12%  | 21.78% | 23.26% | 29.06% | 23.57% | 20%     |
| Alternative Investments | -3.15% | -15.8% | 10.14% | -19.6% | 22.12% | -6.77% | -2%     |
| Nairobi Stock Exchange  | 8.51%  | 17.41% | 20.50% | 14.95% | 21.64% | 17.16% | 16.70%  |

Table 25 shows that Industrial and Allied and Finance and Investments reported the highest revenue growth with an average of 20% during the six years. Meanwhile the worst performing sector is alternative and investments which has reported a general decline of 2% in revenue.

Table 26 provides a summary of the Net Profit Margin for each sector and also the entire market.

**Table 26 - Average Net Profit Margin by Sector**

|                         | 2003   | 2004   | 2005   | 2006   | 2007   | 2008   | Average |
|-------------------------|--------|--------|--------|--------|--------|--------|---------|
| Agriculture             | -10%   | 32%    | -12%   | 13%    | 6%     | 30%    | 10%     |
| Commercial & Services   | 5.36%  | 6.05%  | 7.58%  | 8.44%  | 9.00%  | 5.22%  | 7%      |
| Industrial & Allied     | 5.96%  | 9.81%  | 11.22% | 9.43%  | 10.18% | 9.42%  | 9%      |
| Finance & Investment    | 26.23% | 26.45% | 32.98% | 40.24% | 38.59% | 37.44% | 34%     |
| Alternative Investments | 4.83%  | 6.29%  | 5.89%  | 3.92%  | 6.68%  | -8.57% | 3%      |
| Nairobi Stock Exchange  | 9.92%  | 15.09% | 14.13% | 17.38% | 17.04% | 16.43% | 15.00%  |

Table 26 also shows the Finance and Investment to be the best in terms of Net profit margin with an average of 34% while Alternative Investments has reported the lowest.

Table 27 shows the average Return on Investment by sector and also the total.

**Table 27 - Average Return on Investment by Sector**

|                         | 2003   | 2004   | 2005   | 2006  | 2007   | 2008   | Average |
|-------------------------|--------|--------|--------|-------|--------|--------|---------|
| Agriculture             | -4.6%  | 18%    | 0.4%   | 13%   | 10%    | 19%    | 9%      |
| Commercial & Services   | 5.76%  | 7.38%  | 9.11%  | 9.69% | 9.87%  | 7.35%  | 8%      |
| Industrial & Allied     | 5.46%  | 10.55% | 11.58% | 8.72% | 10.13% | 9.69%  | 9%      |
| Finance & Investment    | 2.26%  | 2.59%  | 2.88%  | 3.87% | 3.74%  | 2.95%  | 3%      |
| Alternative Investments | -0.90% | 2.44%  | 4.72%  | 2.72% | 4.29%  | -4.37% | 1%      |
| Nairobi Stock Exchange  | 3.32%  | 7.26%  | 7.20%  | 7.01% | 7.52%  | 6.42%  | 6.45%   |

Table 27 shows that Agriculture and Industrial and Allied are the best sectors in terms of return on investment with an average of 9%. Alternative investment has reported the lowest at 1%.

Table 28 shows the average Return on Equity by sector and also in total.

**Table 28 Average Return on Equity by Sector**

|                         | 2003   | 2004   | 2005   | 2006   | 2007   | 2008   | Average |
|-------------------------|--------|--------|--------|--------|--------|--------|---------|
| Agriculture             | -5.1%  | 12%    | -1%    | 8%     | 6%     | 11%    | 5%      |
| Commercial & Services   | 16.07% | 18.67% | 18.94% | 20.12% | 19.95% | 7.22%  | 17%     |
| Industrial & Allied     | -11.3% | 16.47% | 19.13% | 15.65% | 18.88% | 18.42% | 13%     |
| Finance & Investment    | 14.18% | 14.39% | 15.98% | 19.18% | 18.38% | 15.97% | 16%     |
| Alternative Investments | -203%  | 3.98%  | 9.75%  | 6.18%  | 7.45%  | -8.40% | -31%    |
| Nairobi Stock Exchange  | -14.3% | 15.46% | 15.90% | 16.44% | 17.30% | 13.48% | 10.72%  |

The table shows that Commercial and services had the best Return on Equity at 17% closely followed by Finance and investment. Alternative Investment was still the worst with a negative return on equity.

Table 4.33 also shows the general performance in terms of share prices by sector and also in total.

**Table 29 - Average Share Price Growth by sector**

|                         | 2003   | 2004  | 2005  | 2006   | 2007   | 2008  | Average |
|-------------------------|--------|-------|-------|--------|--------|-------|---------|
| Agriculture             | 44%    | 92%   | 65%   | 27%    | -35%   | -35%  | 26%     |
| Commercial & Services   | 182%   | 33.0% | 41.5% | 97.4%  | -7.8%  | -7.9% | 56%     |
| Industrial & Allied     | 212.0% | 52.3% | 60.3% | 24.0%  | -9.9%  | -     | 54%     |
|                         |        |       |       |        |        | 14.5% |         |
| Finance & Investment    | 435.3% | 1.2%  | 38.6% | 113.2% | -21.6% | -     | 90%     |
|                         |        |       |       |        |        | 28.8% |         |
| Alternative Investments | 9.5%   | 7.9%  | 21.4% | 41.4%  | 10.1%  | -     | 7%      |
|                         |        |       |       |        |        | 46.8% |         |
| Nairobi Stock Exchange  | 236.7% | 34.4% | 48.1% | 63.7%  | -13.1% | -     | 58.0%   |
|                         |        |       |       |        |        | 21.4% |         |

The general trend in share prices has been on a decline. However Finance and Investment reported the best performance in terms of share price growth. Table 30 provides a summary of the earnings per share by sector.

**Table 30 - Average Earnings per Share by sector (sh.)**

|                         | 2003  | 2004 | 2005  | 2006  | 2007  | 2008  | Average |
|-------------------------|-------|------|-------|-------|-------|-------|---------|
| Agriculture             | -0.77 | 8.90 | -3.95 | 3.24  | 3.82  | 6.59  | 2.97    |
| Commercial & Services   | 2.40  | 2.97 | 4.69  | 4.56  | 5.16  | 3.07  | 3.81    |
| Industrial & Allied     | -0.01 | 3.57 | 5.70  | 6.05  | 7.00  | 7.10  | 4.90    |
| Finance & Investment    | 2.378 | 2.18 | 3.075 | 4.255 | 4.785 | 4.558 | 3.54    |
| Alternative Investments | 0.69  | 6.40 | 6.09  | -2.31 | 5.93  | -8.84 | 1.33    |
| Nairobi Stock Exchange  | 1.09  | 3.74 | 4.05  | 4.38  | 5.71  | 4.32  | 3.88    |

The table shows that the best sector with the highest Earnings per share is Industrial and allied while the lowest was the alternative investments.

A general comparison across sectors has shown that firms in the Finance and Investment sector (followed closely by Industrial and Allied) have performed relatively well in terms of firm performance. The two sectors have also reported an average increase in remuneration over the years. The companies in the Finance and Investment sector comprising largely of banks have been reporting good performance in recent years (OECD, 2008). The sector has also reported the highest average remuneration (at ksh. 48.3million) followed closely by Commercial and Allied at ksh.43.35 million. The worst performing sector is the Alternative Investments in terms of both general profitability and remuneration. The sector paid the lowest average remuneration of ksh. 8.87 million. This is justified because companies classified in this sector are not expected to perform better than the companies in the

Main Investment Market of the stock exchange due to different listing requirements(NSE Handbook, 2002).

Table 31 summarises the betas and the P values for each company, the sector and the entire stock market.

**Table 31 - Remuneration Vs Firm performance - summary**

|                       |              | Remuneration Vs |         |         |         |          |           |
|-----------------------|--------------|-----------------|---------|---------|---------|----------|-----------|
|                       |              | REV GR (%)      | NPM (%) | ROI (%) | ROE (%) | SPG (%)  | EPS (sh.) |
| Kakuzi                | $\beta$      | -0.0929         | -0.5812 | -0.9327 | -0.4342 | 0.08591  | -0.8461   |
|                       | P( $\beta$ ) | 0.714           | 0.171   | 0.193   | 0.261   | 0.049    | 0.152     |
| Rea Vipingo           | $\beta$      | -0.3793         | 0.5675  | 0.5785  | 0.3609  | -0.1238  | 5.822     |
|                       | P( $\beta$ ) | 0.46            | 0.544   | 0.575   | 0.541   | 0.039    | 0.203     |
| Sasini                | $\beta$      | 0.00615         | 0.01648 | 0.0772  | 0.06125 | -0.0302  | -0.0626   |
|                       | P( $\beta$ ) | 0.954           | 0.65    | 0.55    | 0.554   | 0.266    | 0.713     |
| Car & General Kenya   | $\beta$      | 0.11876         | 0.0413  | 0.1827  | 0.2876  | -0.0078  | 1.2766    |
|                       | P( $\beta$ ) | 0.164           | 0.938   | 0.756   | 0.329   | 0.398    | 0.005     |
| CMC Holdings          | $\beta$      | 0.10372         | 2.3206  | 0.6959  | 0.8834  | -0.0157  | -0.932    |
|                       | P( $\beta$ ) | 0.223           | 0.001   | 0.001   | 0.001   | 0.228    | 0.247     |
| Kenya Airways         | $\beta$      | -0.9229         | -6.1961 | -7.52   | -1.9312 | -0.0705  | -4.5286   |
|                       | P( $\beta$ ) | 0.231           | 0.001   | 0.007   | 0.007   | 0.285    | 0.009     |
| Marshalls East Africa | $\beta$      | 0.092           | 0.2965  | 0.3505  | 0.07328 | 0.00689  | 0.3856    |
|                       | P( $\beta$ ) | 0.461           | 0.189   | 0.219   | 0.227   | 0.786    | 0.188     |
| Nation Media Group    | $\beta$      | 4.087           | 1.69    | 5.248   | 3.822   | -0.0706  | 2.554     |
|                       | P( $\beta$ ) | 0.057           | 0.887   | 0.475   | 0.258   | 0.748    | 0.727     |
| Standard Group        | $\beta$      | 0.0811          | -0.534  | -0.022  | -1.0247 | -0.0093  | 0.343     |
|                       | P( $\beta$ ) | 0.832           | 0.815   | 0.992   | 0.028   | 0.871    | 0.941     |
| TPS Serena            | $\beta$      | -0.05374        | 0.9638  | 1.008   | 0.4983  | -0.1317  | 1.957     |
|                       | P( $\beta$ ) | 0.559           | 0.178   | 0.442   | 0.49    | 0.017    | 0.321     |
| Athi River Mining     | $\beta$      | 0.305           | 0.327   | 0.533   | 0.7889  | -0.07073 | 9.858     |
|                       | P( $\beta$ ) | 0.633           | 0.896   | 0.863   | 0.445   | 0.22     | 0.007     |
| Bamburi Cement        | $\beta$      | 1.455           | 2.655   | 3.34    | 2.44    | -0.15    | 6.225     |
|                       | P( $\beta$ ) | 0.029           | 0.457   | 0.16    | .006    | .096     | .006      |
| BOC Kenya             | $\beta$      | -0.01188        | 0.2996  | -0.0556 | -0.1907 | 0.026984 | -0.4232   |
|                       | P( $\beta$ ) | 0.91            | 0.71    | 0.956   | 0.803   | 0.018    | 0.587     |
| BAT                   | $\beta$      | 1.6             | -9.071  | -2.783  | 6.223   | -0.1331  | 20.69     |
|                       | P( $\beta$ ) | 0.496           | 0.148   | 0.413   | 0.35    | 0.3      | 0.006     |
| Crown-Berger (Kenya)  | $\beta$      | -0.0282         | -1.377  | -1.558  | -0.788  | -0.0139  | 0.355     |
|                       | P            | 0.859           | 0.522   | 0.417   | 0.549   | 0.49     | 0.932     |
| Mumias Sugar          | $\beta$      | 0.3722          | 2.7421  | 2.7773  | 1.7574  | -0.00785 | 10.217    |
|                       | P( $\beta$ ) | 0.579           | 0.005   | 0.015   | 0.015   | 0.93     | 0.094     |
| EA Portland Cement    | $\beta$      | -0.0674         | 0.474   | 0.912   | 0.3591  | -0.04941 | 0.181     |
|                       | P( $\beta$ ) | 0.863           | 0.679   | 0.501   | 0.476   | 0.046    | 0.844     |
| East African          | $\beta$      | 2.192           | 3.83    | 5.198   | 3.002   | -0.3356  | 12.043    |

|                       |              |          |         |         |         |          |         |
|-----------------------|--------------|----------|---------|---------|---------|----------|---------|
| Breweries             | P( $\beta$ ) | 0.308    | 0.113   | 0.038   | 0.101   | 0.07     | 0.045   |
| KPLC                  | $\beta$      | 0.1304   | 0.5307  | 0.8189  | 0.04016 | -0.04002 | 0.19442 |
|                       | P( $\beta$ ) | 0.42     | 0.092   | 0.061   | 0.037   | 0.101    | 0.068   |
| Kenya Oil             | $\beta$      | 0.0594   | -5.45   | -1.2636 | -0.8777 | -0.0234  | 1.899   |
|                       | P( $\beta$ ) | 0.249    | 0.049   | 0.146   | 0.127   | 0.439    | 0.357   |
| East African Cables   | $\beta$      | -0.00424 | 0.2304  | -0.0561 | 0.0349  | -0.02469 | 1.828   |
|                       | P( $\beta$ ) | 0.966    | 0.706   | 0.899   | 0.889   | 0.296    | 0.689   |
| Sameer Group          | $\beta$      | 0.0846   | 0.1112  | 0.1369  | -0.0132 | -0.02037 | -0.781  |
|                       | P            | 0.668    | 0.908   | 0.88    | 0.983   | 0.742    | 0.926   |
| Total Kenya           | $\beta$      | -0.14686 | -9.937  | -4.51   | -0.682  | -0.0567  | 2.096   |
|                       | P( $\beta$ ) | 0.195    | 0.137   | 0.087   | 0.807   | 0.225    | 0.805   |
| Unga Group            | $\beta$      | 0.1259   | -0.7509 | -0.3916 | -0.2301 | 0.00081  | -0.826  |
|                       | P            | 0.427    | 0.321   | 0.345   | 0.334   | 0.969    | 0.342   |
| Barclays              | $\beta$      | 0.2634   | -0.6536 | -3.317  | -2.4974 | -0.0267  | 5.141   |
|                       | P( $\beta$ ) | 0.173    | 0.12    | 0.618   | 0.05    | 0.357    | 0.189   |
| Centum Investment     | $\beta$      | 0.003578 | -0.0022 | 0.0924  | 0.0965  | 6.2E-06  | 0.4136  |
|                       | P( $\beta$ ) | 0.598    | 0.825   | 0.435   | 0.441   | 0.986    | 0.417   |
| Diamond Trust Bank    | $\beta$      | 0.19237  | 0.2849  | 2.86    | 0.5656  | -0.0423  | 2.2058  |
|                       | P( $\beta$ ) | 0.091    | 0.331   | 0.804   | 0.519   | 0.153    | 0.02    |
| Housing Finance       | $\beta$      | 0.00569  | 1.783   | -0.3527 | -0.0047 | 1.166    | 0       |
|                       | P( $\beta$ ) | 0.891    | 0.694   | 0.693   | 0.608   | 0.854    | 0       |
| Jubilee Insurance     | $\beta$      | -0.0164  | 0.941   | -5.79   | -1.7051 | 0.03274  | -1.3611 |
|                       | P( $\beta$ ) | 0.878    | 0.653   | 0.608   | 0.084   | 0.246    | 0.222   |
| KCB                   | $\beta$      | 0.8112   | 2.4594  | 29.459  | 3.7325  | -0.154   | 35.158  |
|                       | P( $\beta$ ) | 0.044    | 0.019   | 0.013   | 0.003   | 0.14     | 0.004   |
| NBK                   | $\beta$      | -0.1461  | 1.1398  | 17.176  | 2.556   | -0.0878  | 7.103   |
|                       | P( $\beta$ ) | 0.71     | 0.017   | 0.01    | 0.224   | 0.087    | 0.004   |
| NIC Bank              | $\beta$      | 0.2479   | 0.264   | 7.17    | 2.222   | -0.1324  | 3.865   |
|                       | P( $\beta$ ) | 0.24     | 0.84    | 0.617   | 0.131   | 0.089    | 0.519   |
| Pan Africa Insurance  | $\beta$      | 0.1384   | 0.188   | 0.5856  | 0.1408  | -0.0489  | 0.591   |
|                       | P( $\beta$ ) | 0.712    | 0.57    | 0.586   | 0.616   | 0.183    | 0.593   |
| SCB                   | $\beta$      | 0.4192   | -0.463  | -6.66   | -0.837  | -0.0327  | -4.314  |
|                       | P( $\beta$ ) | 0.354    | 0.68    | 0.685   | 0.541   | 0.75     | 0.328   |
| Express Kenya         | $\beta$      | 0.19453  | -0.3312 | -0.2918 | -       | -0.05351 | -0.2763 |
|                       | P( $\beta$ ) | 0.021    | 0.523   | 0.459   | 0.455   | 0.324    | 0.538   |
| Williamson Tea Kenya  | $\beta$      | -0.02401 | 0.0966  | 0.1852  | 0.1243  | 0.01843  | 0.0894  |
|                       | P            | 0.718    | 0.645   | 0.78    | 0.785   | 0.688    | 0.541   |
| Agriculture           | $\beta$      | -0.07    | -0.02   | 0.19    | 0.15    | 0.18     | -0.21   |
|                       | P            | 0.673    | 0.845   | 0.452   | 0.37    | 0.606    | 0.528   |
| Commercial & Services | $\beta$      | 0.004    | 1.3     | 1.44    | 0.704   | -0.02    | 2.2     |
|                       | P            | 0.984    | 0.146   | 0.084   | 0.016   | 0.614    | 0.07    |
| Industrial & Allied   | $\beta$      | -0.143   | 3.97    | 4.2     | 0.33    | -0.06    | 1.69    |
|                       | P            | 0.434    | 0.00    | 0.00    | 0.26    | 0.162    | 0.024   |
| Finance & investments | $\beta$      | -0.05    | -0.02   | -1.33   | 1.9     | -0.015   | 2.84    |
|                       | P            | 0.727    | 0.817   | 0.422   | 0.00    | 0.212    | 0.009   |

|                         |         |        |       |       |        |        |       |
|-------------------------|---------|--------|-------|-------|--------|--------|-------|
| Alternative Investments | $\beta$ | -0.019 | 0.16  | 0.039 | -0.013 | 0.0121 | 0.033 |
|                         | P       | 0.789  | 0.539 | 0.918 | 0.27   | 0.79   | 0.869 |
| Nairobi Stock Exchange  | $\beta$ | 0.015  | 0.317 | 2.4   | 0.14   | -0.015 | 1.6   |
|                         | P       | 0.89   | 0.06  | 0.01  | 0.06   | 0.25   | 0.02  |

Table 32 shows a summary of directors' remuneration as a percentage of revenue in the Agricultural sector.

**Table 32 - Remuneration as a percentage of revenue- Agriculture**

|                           | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | Average |
|---------------------------|------|------|------|------|------|------|---------|
| Kakuzi                    | 1.21 | 1.87 | 1.84 | 1.08 | 0.93 | 0.14 | 1.18    |
| Rea Vipingo Sisal Estate  | 1.50 | 1.41 | 1.49 | 1.26 | 2.36 | 2.33 | 1.73    |
| Sasini Tea and Coffee     | 0.16 | 0.38 | 0.75 | 0.56 | 0.68 | 0.70 | 0.54    |
| <b>Average for sector</b> | 0.96 | 1.22 | 1.36 | 0.97 | 1.32 | 1.06 | 1.15    |

In relative terms Rea Vipingo paid 1.73% of its revenues to directors over the period under study which was the highest in the sector. This is followed by Kakuzi with 1.18% and finally Sasini with a low of 0.54%. The ratio has been on an upward trend in the sector.

Table 33 shows a summary of directors' remuneration as a percentage of revenue in the Commercial and Services sector.

**Table 33 - Remuneration as a percentage of revenue- Commercial & Services**

|                           | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | Average |
|---------------------------|------|------|------|------|------|------|---------|
| Car & General Kenya       | 1.96 | 1.38 | 1.43 | 1.26 | 0.95 | 0.66 | 1.27    |
| CMC Holdings              | 0.46 | 0.38 | 0.37 | 0.36 | 0.32 | 0.27 | 0.36    |
| Kenya Airways             | 0.47 | 0.36 | 0.19 | 0.16 | 0.15 | 0.16 | 0.25    |
| Marshalls East Africa     | 0.62 | 0.84 | 0.66 | 0.58 | 1.32 | 0.48 | 0.75    |
| Nation Media Group        | 1.01 | 0.77 | 1.20 | 1.40 | 1.42 | 0.85 | 1.11    |
| Standard Group            | 4.30 | 2.55 | 4.48 | 2.50 | 2.57 | 2.35 | 3.13    |
| TPS Serena                | 1.51 | 1.20 | 0.73 | 0.81 | 0.91 | 1.03 | 1.03    |
| <b>Average for sector</b> | 1.48 | 1.07 | 1.29 | 1.01 | 1.09 | 0.83 | 1.13    |

In the commercial and services Standard group paid the highest remuneration at 3.13% with the lowest being Kenya Airways at 0.25%. It appears the trend for the remuneration has been declining from a high of 1.48% to a low of 0.83% over the six years.

Table 34 shows a summary of directors' remuneration as a percentage of revenue in the Industrial and Allied sector.

**Table 34 - Remuneration as a percentage of revenue- Industrial & Allied**

|                           | 2003        | 2004        | 2005        | 2006        | 2007        | 2008        | Average     |
|---------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Athi River Mining         | 1.60        | 1.62        | 1.40        | 2.03        | 1.47        | 1.28        | 1.57        |
| Bamburi Cement            | 0.86        | 0.65        | 0.65        | 0.56        | 0.48        | 0.41        | 0.60        |
| BOC Kenya                 | 3.07        | 1.68        | 1.43        | 1.29        | 1.15        | 1.19        | 1.64        |
| British American Tobacco  | 1.00        | 1.35        | 1.28        | 1.16        | 1.34        | 1.74        | 1.31        |
| Crown-Berger (Kenya)      | 0.94        | 0.69        | 0.50        | 1.30        | 0.89        | 1.03        | 0.89        |
| Mumias Sugar              | 0.08        | 0.46        | 0.46        | 0.43        | 0.51        | 0.46        | 0.40        |
| EA Portland Cement        | 0.10        | 0.49        | 0.39        | 0.31        | 0.25        | 0.28        | 0.30        |
| East African Breweries    | 0.82        | 0.87        | 0.98        | 1.03        | 0.66        | 0.65        | 0.84        |
| Kenya Power and lighting  | 0.05        | 0.10        | 0.11        | 0.06        | 0.06        | 0.06        | 0.07        |
| Kenya Oil                 | 0.05        | 0.03        | 0.03        | 0.03        | 0.02        | 0.02        | 0.03        |
| East African Cables       | 2.15        | 0.64        | 1.11        | 1.11        | 0.17        | 0.30        | 0.91        |
| Sameer Group              | 1.45        | 1.09        | 0.64        | 1.02        | 0.87        | 0.93        | 1.00        |
| Total Kenya               | 0.05        | 0.03        | 0.04        | 0.07        | 0.07        | 0.06        | 0.05        |
| Unga Group                | 0.19        | 0.26        | 0.21        | 0.15        | 0.11        | 0.12        | 0.17        |
| <b>Average for sector</b> | <b>0.89</b> | <b>0.71</b> | <b>0.66</b> | <b>0.75</b> | <b>0.58</b> | <b>0.61</b> | <b>0.70</b> |

BOC Kenya paid the highest remuneration as a percentage of revenue at 1.64% while Kenya oil was the lowest at 0.03%. Again the ratio has also been declining over the years from a high of 0.89% to a low of 0.61%.

Table 35 shows a summary of directors' remuneration as a percentage of revenue in the Finance and investment sector.

**Table 35 - Remuneration as a percentage of revenue- Finance & Investment**

|                            | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | Average |
|----------------------------|------|------|------|------|------|------|---------|
| Barclays Bank of Kenya     | 0.57 | 0.58 | 0.60 | 0.50 | 0.37 | 0.34 | 0.49    |
| Centum Investment          | 6.88 | 4.25 | 6.29 | 3.50 | 2.02 | 2.58 | 4.25    |
| Diamond Trust Bank         | 2.74 | 2.91 | 2.03 | 1.79 | 1.36 | 1.22 | 2.01    |
| Housing Finance Company    | 1.35 | 2.64 | 2.87 | 2.78 | 2.57 | 2.32 | 2.42    |
| Jubilee Insurance          | 1.37 | 1.39 | 1.13 | 0.98 | 0.61 | 0.22 | 0.95    |
| Kenya Commercial Bank      | 1.33 | 1.36 | 1.31 | 1.32 | 1.21 | 0.73 | 1.21    |
| National Bank of Kenya     | 0.56 | 0.71 | 0.75 | 0.76 | 1.21 | 1.32 | 0.88    |
| National Industrial Credit | 3.61 | 3.98 | 2.91 | 1.88 | 1.86 | 1.90 | 2.69    |
| Pan Africa Insurance       | 2.16 | 2.57 | 2.22 | 2.46 | 1.81 | 1.43 | 2.11    |
| Standard Chartered Bank    | 2.40 | 3.11 | 2.45 | 1.85 | 1.78 | 1.17 | 2.13    |
| <b>Average for sector</b>  | 2.30 | 2.35 | 2.26 | 1.78 | 1.48 | 1.32 | 1.91    |

Centum investment paid the highest remuneration as a percentage of revenue in this sector at 4.25%. The lowest was National bank of Kenya at 0.88%. The ratio was on a declining trend over the period under study with a high of 2.35% and a low of 1.32%.

Finally, table 36 shows a summary of directors' remuneration as a percentage of revenue in the Alternative Investment sector.

**Table 36 - Remuneration as a percentage of revenue- Alternative Investment**

|                           | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | Average |
|---------------------------|------|------|------|------|------|------|---------|
| Express Kenya             | 0.42 | 0.34 | 0.85 | 0.97 | 1.95 | 2.24 | 1.13    |
| Kapchorua Tea             | 0.10 | 0.09 | 0.07 | 0.09 | 0.07 | 0.07 | 0.08    |
| Williamson Tea Kenya      | 2.08 | 1.94 | 1.15 | 1.11 | 0.90 | 1.01 | 1.36    |
| <b>Average for sector</b> | 0.87 | 0.79 | 0.69 | 0.72 | 0.97 | 1.11 | 0.86    |

Williamson Tea Kenya paid the highest remuneration as a percentage of revenue at 1.36%, while Kapchorua Tea had the lowest at 0.08%. The ratio has been on an upward trend.

Generally, finance and investment had the best ratio while industrial and allied had the lowest.

### 4.3 Common forms of directors pay

The following results were summarised from the questionnaires:

Question 2 of the questionnaire was phrased as follows:

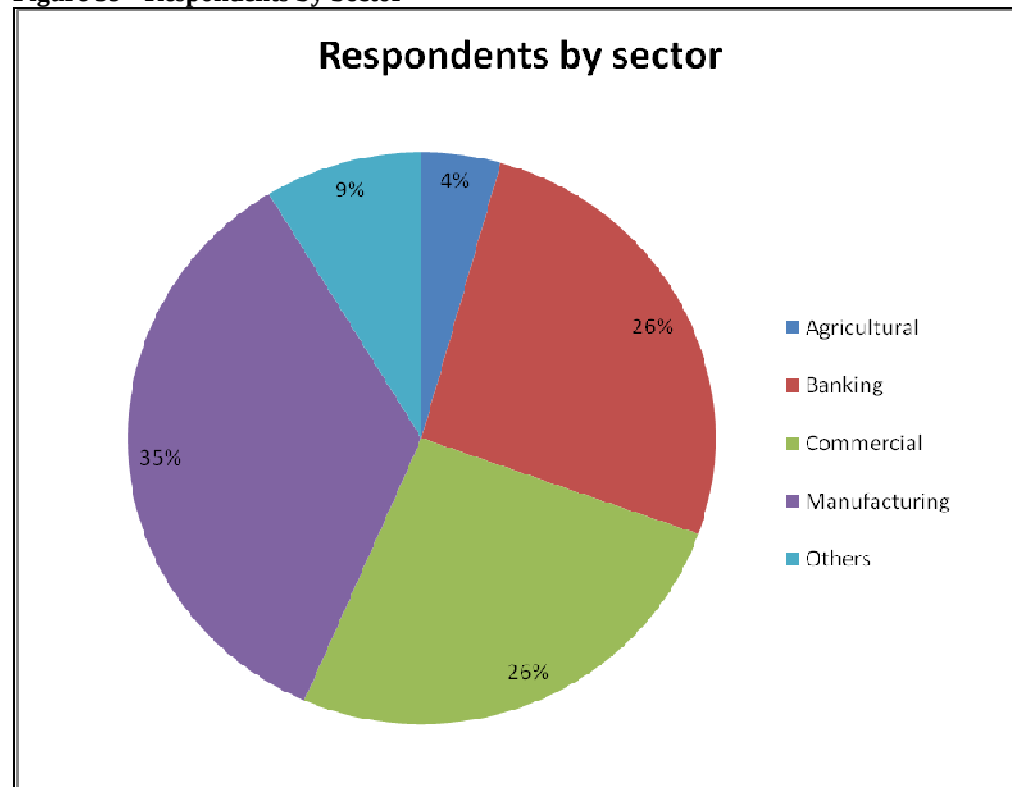
Indicate sector or industry of operation

The summary of the respondents providing information about their main sectors is given in Table 37 and figure 39.

**Table 37 - Respondents by Sector**

|               | No. | %       |
|---------------|-----|---------|
| Agricultural  | 1   | 4.35%   |
| Banking       | 6   | 26.09%  |
| Commercial    | 6   | 26.09%  |
| Manufacturing | 8   | 34.78%  |
| Others        | 2   | 8.69%   |
|               | 23  | 100.00% |

**Figure 39 - Respondents by Sector**



Majority of the respondents did not fill in question 3 on ownership (whether local, foreign or both) and therefore this part was excluded from the analysis.

Question 4 was phrased as follows:

Does the company pay the following to directors?

The response was analysed into sectors and the summary is given in Table 38.

**Table 38 - Common forms of payment by sector**

|                                    | Agriculture | Banking | Commercial | Manuf. | Others | Total |
|------------------------------------|-------------|---------|------------|--------|--------|-------|
| Basic salary and benefits          | 1           | 6       | 6          | 5      | 2      | 20    |
| Short-term benefits – bonus        | 0           | 0       | 0          | 0      | 0      | 0     |
| Long-term benefits – Stock options | 0           | 0       | 0          | 3      | 0      | 3     |
| Entry benefits – golden hello      | 0           | 0       | 0          | 0      | 0      | 0     |
| Exit benefits – golden bye bye     | 0           | 0       | 0          | 0      | 0      | 0     |

An analysis of the questionnaires revealed that all the companies pay their directors salaries and other short term benefits including pension contributions (both defined benefit and defined contribution schemes). About 12.5% of the companies pay the directors stock options and none of the companies paid neither a bonus nor any other benefits like entry or exit benefits. The 20% companies were mainly from the industrial and allied sectors of the Nairobi Stock Exchange.

However it was noted that some of the respondents operate an employee stock ownership scheme in which the directors are also eligible to participate.

The study did not analyse the forms of payment across sectors as no response was received from alternative investments. The study was also not able to analyze forms of executive pay based on ownership because data was not comprehensive.

#### **4.4 Key factors that determine executive pay**

Question 4 was phrased as follows;

Are the following factors considered by the company when determining directors' remuneration?

The response was summarised in Table 39.

**Table 39 - Factors considered in determining director's remuneration**

| Qualifications   | Agriculture | Banking | Commercial | Manufacturing | Others | Total |
|------------------|-------------|---------|------------|---------------|--------|-------|
| Yes              | 1           | 6       | 6          | 8             | 2      | 23    |
| No               | 0           | 0       | 0          | 0             | 0      | 0     |
| Experience       |             |         |            |               |        |       |
| Yes              | 1           | 6       | 6          | 8             | 2      | 23    |
| No               | 0           | 0       | 0          | 0             | 0      | 0     |
| Age              |             |         |            |               |        |       |
| Yes              | 1           | 6       | 6          | 8             | 2      | 23    |
| No               | 0           | 0       | 0          | 0             | 0      | 0     |
| Firm performance |             |         |            |               |        |       |
| Yes              | 1           | 6       | 6          | 8             | 2      | 23    |
| No               | 0           | 0       | 0          | 0             | 0      | 0     |
| Tax              |             |         |            |               |        |       |
| Yes              | 0           | 2       | 2          | 1             | 0      | 5     |
| No               | 1           | 4       | 4          | 7             | 2      | 18    |

All the respondents consider Qualifications, Experience, Age and Firm performance to be the key factors that influence executive pay. Only about 30% of the respondents considered tax to be an issue, although some commented that this was a problem for the executive and not the company. A respondent explained that the reason why they may not pay stock options was due to the tax implications. An employee (in this case also a director) is taxed on the difference between the exercise price on the stock option and the market price of the company's share being taken as the benefit.

Question 6 was phrased as follows:

Which one of the above factors in Question five is considered important in determining directors pay?

The response was also summarized in Table 40.

**Table 40 - Ranking of important factors in determining executive pay**

|                  | No. | %       |
|------------------|-----|---------|
| Qualifications   | 7   | 30.43%  |
| Experience       | 14  | 60.87%  |
| Age              | 0   | 0.00%   |
| Firm performance | 2   | 8.7%    |
| Tax              | 0   | 0.00%   |
|                  | 23  | 100.00% |

When asked to rank the key factors in order of importance, 61% of the respondents ranked experience to be the most important followed by qualifications (Academic and Professional) and then firm performance. Only 30% of the respondents thought qualifications were important then experience. On enquiry, some respondents claimed that corporate governance practices now recommend appointment of qualified directors although experience is also very important. 9% of the respondents ranked firm performance and experience as important and gave them equal prominence. One respondent highlighted that firm performance is usually considered when they evaluate the overall performance of a director though not necessarily to make decisions on executive remuneration.

## **CHAPTER FIVE: DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS**

### **5.1 Introduction**

The objective of this chapter is to summarise the key issues from the findings in the previous section. Please note that due to the number of companies involved in this study, part of the discussions have been done in chapter four. This chapter will also discuss the general conclusions of the study, the limitations and finally, the recommendations for further studies.

### **5.2 Discussions**

The findings have provided very important information specifically for each company, across the sectors and at a general level for the Nairobi Stock Exchange companies. Generally performance of the companies was good apart from a few

that were adversely affected by the post election violence in 2008. Performance from year 2003 up to 2007 improved as a result of a good economic environment. Apart from poor weather conditions and unstable exchange rates, most companies explained the economy was good for business up to early 2008.

Generally, directors' remuneration has increased across all the sectors except that of alternative investments even though on average the number of directors has remained the same over the period under study. The best sector in terms of paying directors' remuneration is that of Finance and Investment followed by Commercial and Services with the worst performing being the Alternative investment. The average directors' remuneration for the entire NSE is ksh.39 million.

Industrial and Allied and Finance and Investments reported the highest revenue growth with an average of 20% during the six years. Meanwhile the worst performing sector is alternative and investments which has reported a general decline of 2% in revenue. Finance and Investment is the best in terms of Net Profit Margin with an average of 34% while Alternative Investments has reported the lowest.

Agriculture and Industrial and Allied are the best sectors in terms of Return on Investment with an average of 9%. Alternative Investment has reported the lowest at 1%. The general trend in share prices has been on a decline. However Finance and Investment reported the best performance in terms of share price growth.

A general comparison across sectors has shown that firms in the Finance and Investment sector (followed closely by Industrial and Allied) have performed relatively well. The two sectors have also reported an average increase in remuneration over the years. The companies in the Finance and Investment sector comprising largely of banks have been reporting good performance in recent years (OECD, 2008). The sector has also reported the highest average remuneration 48.3million followed by commercial and allied closely at sh.43.35 million. The worst performing sector is Alternative Investments in terms of both general profitability and remuneration. The sector paid the lowest average remuneration of sh. 8.87 million. Companies classified in this sector have less strict rules with regards to performance and position as compared to those in Main Investment Market of the stock exchange (NSE, 2002).

A few important observations noted about the companies are that only Kenya Airways showed a negative relationship between remuneration and firm performance across all the performance variables. Most of the of the other companies had mixed results but if we exclude share price growth, Car and General, Nation , Mumias, East African Breweries, Diamond bank, Kenya Commercial Bank, Athi River and Bamburi show a positive relation between firm performance and remuneration but Kenya Commercial Bank is the only company to show a significant relation. Excluding share price again Kakuzi is the only company that reported a negative relationship between firm performance and remuneration though this is not very significant.

Still at individual company analysis, a count of the 36 companies whose data has been analysed by regression shows that 24 companies (67%) reported a positive relation between Remuneration and Revenue Growth and Net Profit Margin, with the balance of (12) 33% reporting a negative relation. However, none of these relationships were strong (significant). Meanwhile 22 companies (61%) reported a positive relationship between Remuneration and Return on Investment and Return on Equity. The balance

of 14 (39%) had a negative relationship and only one company reported a significant positive relation. Meanwhile 26 companies (72%) reported a positive relationship between Remuneration and Earnings per Share out of which three companies had a significant positive relation. The balance of (10) 28% showed a negative relationship between Remuneration and Earnings per Share. Finally 19 companies (53%) reported a negative relationship between Remuneration and Share Price Growth while 17 (47%) reported a negative relation with no company reporting a strong relationship.

A general regression analysis has shown that for all the companies used, remuneration has a negative relationship with share price but positive relation with Revenue growth, Net Profit Margin, Return on Investment and Return on Equity. For Earnings Per Share the relationship varied from one period to the next. The overall remuneration has also increased from an average of sh.28.55 million in 2003 to sh.44.85 million in 2008 representing approximately 60% increase over the six years. This is in agreement with Carol and Saks (2005) who explained that executive remuneration in several countries has been on the increase.

An important observation from the graphs was a general pattern for internal performance indicators for Revenue growth, Net Profit Margin, Return on Investment and Return on Equity showing that they all tended to move in the same direction. This feature may imply that it is possible to identify one or two variables to be used as internal measures of firm performance for example revenue growth and return on equity. But when analysed individually, by sector or in total, the findings show mixed relations of either positive or negative relations between executive remuneration and each of the variables of firm performance. This means that even though the internal performance indicators show a general pattern, when regressed with executive remuneration, the results were different. However there was no evidence that these were significant apart from a few companies that have already been highlighted.

Even though the study expected a positive strong relationship between firm executive remuneration and firm performance, the findings show a positive but not a strong relationship. The study is in agreement with other studies that found a positive relationship between executive pay and firm performance but the relationship is weak or not significant (Kubo, 2001; Hasssan, Christopher, Evans, 2003; Ozkan, 2007).

The study does not support some prior studies that found a strong positive relationship between executive pay and firm performance (Joskow and Rose, 1994; Kato and Long, 2006; Buck, Liu and Skovoroda, 2008)).

The study has also confirmed the initial recommendations by Combs and Skill,(2003) who explained that in addition to firm performance, remuneration committees consider the directors experience, age and qualifications (academic and professional). Unfortunately the study did not find tax an important aspect in designing executive remuneration as stated by Rose and Wolfram (2002).The study found evidence of a relationship between executive remuneration and firm size like in the studies of Aditya, Debashish and Krsihnakumar (2006) and Shah, Javed and Abbas (2009)

The study is in agreement with some of the findings by Boyd (1996) on key determinants of executive pay apart from the experience, age, qualification and tax. Even though experience age and qualifications are some key determinants of executive remuneration, unfortunately the study did not find any relationship between remuneration and firm size and firm profitability. Boyd explained that as expected executive remuneration is higher for firms with large size, high profits, smaller shareholder concentration and competent board. The study did not compare shareholder concentration and board competence.

### 5.3 Conclusions

The study has provided more empirical evidence regarding executive remuneration and firm performance for Nairobi Stock Exchange companies.

The study has established the nature of the relationship between executive pay and firm performance by first deriving the Null hypothesis that was stated as follows:

$H_0$ : There is no strong positive relationship between executive remuneration and firm performance

From both the individual and sector analysis, executive remuneration has generally been increasing but firm performance has tended to stabilise and in some cases declined. The regression analysis has shown mixed relationships between executive remuneration and Revenue Growth, Net Profit Margin, Return on Investment, Return on Equity, Earnings per share and Share Price Growth with some being positive and some negative. Majority of the companies have reported positive relationship between executive remuneration and all the performance indicators (except for Share Price Growth). The null hypothesis could not be rejected and therefore the study did not find a strong positive relationship between executive pay and firm performance.

This is also supported by respondents who have given a major indication that most of the companies listed on the Nairobi Stock Exchange consider experience to be the most important factor in designing executive pay followed by qualifications (Academic and professional).

## **5.4 Limitations of the research**

The initial objective of the study was to consider all the companies that are quoted on the Nairobi stock Exchange i.e. about 58 as at 31 December 2008 (NSE Handbook, 2008). But the number was reduced to those companies that were quoted from 2003 up to 2008 which were about 43. The companies that were quoted during the period under analysis were required because of the share price that was one of the external measures of firm performance.

Another challenge was also in the process of collecting data. This is because even though Nairobi Stock Exchange companies are required to present copies of their financial statements to the various regulators, some companies do not do the same. Obtaining copies of the same proved difficult and this reduced the number of companies to be analysed to 37. A few companies also have online financial statements and some effort had to be made in collecting the physical copies for those without online copies. Despite these challenges the financial statements for the 37 companies was still considered a good source of information for the analysis.

An additional limitation is in the information that NSE companies disclose regarding directors and their remuneration. There is inconsistency in disclosure regarding the number of executive and non executive directors. In addition it is not clear how much of the fees paid to directors relate to non executive and executive. However the basic assumption of the study is that the amount paid to non executive directors is insignificant. Non executive directors also have an indirect contribution to firm performance.

Additional limitations arose in getting respondents to fill in the questionnaire where there was lack of cooperation (not available, very busy) and no response policy. Some attempts were made to replace the respondents who operate a no response policy so as to increase the response rate. There are limitations also on the tool of analysis i.e. regressions and questionnaires. For example regression analysis has some assumptions like linearity between the dependent and independent variables. This means that the study assumes that there is a linear relationship between firm performance and executive remuneration. However regression is one of the best tools to use in studying relationships among different variables. Furthermore, there was no assumption of causality i.e. high executive pay leads to better firm performance.

## **5.5 Recommendations**

### **5.5.1 Importance of findings**

The findings of the study are very important because of several reasons. If there is no evidence of a strong positive relationship between firm performance and executive pay for NSE companies, then for the purpose of agency theory, there is a high chance of directors benefiting at the expense of shareholders. For example in the analysis, some companies' executive remuneration has been increasing while performance indicators show a declining level of performance. This raises questions mainly for investors, companies and regulators. Investors will need to consider this implication in their decision making process. Shareholders will have to be more sensitized especially on corporate governance principles. It will be important to determine what issues investors consider when evaluating the performance of the executives and companies and whether they are aware about their critical role in corporate governance.

Within companies, it is important to establish what challenges the remuneration committees and even companies are faced with in coming up with executive remuneration and whether they are really practical in the local context.

For regulators, it appears that Nairobi Stock Exchange companies are yet to implement some aspects of good corporate governance principles. Even though the companies have a remuneration committee, firm performance is not a very important consideration in determining executive pay. It is important to find out what are the key challenges of implementing pay based performance schemes for executives so that they are addressed. Furthermore regulators will need to establish other means of enforcing pay based on performance.

The study has also been useful for academicians and other researchers. Issues to do with executive pay will continue to be a major area of discussion and new dimensions will arise as companies evolve. In US and Europe, a lot of attention has been given to executive pay and firm performance. A major issue that arises for researchers is that there is no evidence of a relationship between firm performance and executive

remuneration for NSE companies yet this is not a major source of worry for regulators and investors locally. A question that arises is whether pay for performance measures for executives is practicable in an emerging economy or for local companies or this requirement can be applied with exceptions.

### **5.5.2 Suggestions for further research**

First because of the limitations of the study mainly the reduced number of companies, an additional research can be carried out that applies the same to all the companies of the Nairobi Stock Exchange that have provided financial statements but not necessarily been quoted during the period. However focus can be on internal measures of performance (exclude the Share Price Growth). Furthermore the study can also try and establish the practical challenges of implementing performance based payment for Nairobi Stock Exchange companies. Even though the study highlighted the same, there may be other practical challenges that would be of interest to regulators and researchers.

Additional studies can be carried out in the region so as to find out if this is the same case. This can raise the question on whether pay for performance can be practical or a revision is required in the corporate governance principles based on the findings.

Meanwhile researchers can also focus on executive pay, firm performance and corporate governance practices in the public sector (performance contracting) and small and medium sized firms to determine whether there are any unique attributes about the same.

## BIBLIOGRAPHY

Aditya P., Debashish, B and Menon, Krishnakumar M. (2006), Executive Compensation, Firm Performance and Corporate Governance: An Empirical Analysis. Available at SSRN: <http://ssrn.com/abstract=881730>, Last accessed 16 November 2009.

Akst, D. (2006), Why Rules Can't Stop Executive Greed, *New York Times*, available at: [http://www.nytimes.com/2006/03/05/business/yourmoney/05cont.html?\\_r=1](http://www.nytimes.com/2006/03/05/business/yourmoney/05cont.html?_r=1) Last accessed 18 August 2009.

Anderson, M. C., Banker, R.D. and Ravindran, S. (2000), Executive Compensation in the Information Technology Industry. *Management Science*, Vol. 46, No.4, pp.530-547.

Antle, R. and Smith, A. (1986), An empirical investigation of the relative Performance Evaluation of Corporate Executives, *Journal of Accounting Research*, Vol. 24, pp. 1-39.

Bacidore, J. M., A. Boquist, J. A., Milbourn, T. T. and Thakor, A.V. (1997), The Search for the Best Financial Performance Measure, *Financial Analysts Journal*, Vol. 53, No. 3, pp. 11-20.

Barro, J. R. and Barro, R.J. (1990), Pay, Performance, and Turnover of Bank CEOs, *Journal of Labor Economics*, Vol. 8, No. 4 , pp. 448-481.

Bebchuk, L. A. and Fried, J. M. (2003), Executive Compensation as an Agency Problem, *Journal of Economic Perspectives*, Vol. 17, No.3, pp.71-92.

Bebchuk, L. A. and Fried, J. M. (2004), Pay Without Performance: The Unfulfilled Promise of Executive Compensation, *Journal of Economic Literature*, Vol. 45, No.2, pp.419-428.

Berle, A. and Means, G. (1932), *The Modern Corporation and private property*. New York: Macmillan.

Bhagat, S. and Bolton, B. (2008), Corporate Governance and Firm Performance, *Journal of Corporate Finance*, Vol.14, pp.257, 264-69.

Bocean, C.G. and M. Barbu, C.M. (2007), Corporate governance and firm performance, Available at: <http://www.mnmk.ro/documents/2007/2007-14.pdf> Accessed 25 June 2009.

Boyd, B.K. (1996), Determinants of US Outside Director Compensation, *Corporate Governance: An International Review*, Vol. 4, No.4, pp.202-211.

Bratton, W. W. (2005), The Academic Tournament over Executive Compensation. *California Law Review*, 93(5).

- Brick, I. E., Palmon, O., and K. Wald, J.K. (2005), CEO compensation, director compensation, and firm performance: Evidence of cronyism?, *Journal of Corporate Finance*, Vol. 12, No. 3, pp. 403-423.
- Brown, K.C. and Reilly, F.K., (2009), *Analysis of Investments and management of Portfolios*, 9<sup>th</sup> edition, South-Western Cengage Learning
- Brunello, G., Graziano, C. and B. Parigi (2001), Executive compensation and firm performance in Italy, *International Journal of Industrial Organization*, Vol. 19, pp. 133–161.
- Buck, T., Liu, X. and Skovoroda, R. (2008), Top executive pay and firm performance in China, *Journal of International Business Studies*, Vol. 39, No.5, pp.833-850.
- CA 1962, Laws of Kenya: Chapter 486: Companies Act, Government Printer, Nairobi
- Caramanolis-Cötelli, B. (1995), “External and Internal Corporate Control Mechanisms and the Role of the Board of Directors: A Review of the Literature”, *Working Paper. nr. 9606*, Institute of Banking and Financial Management.
- Carola, F. and Saks, R.E. (2005), “Historical Trends in Executive Compensation, 1936-2003.” Mimeograph (November).
- Chan, M., (2008), Executive Compensation. *Business and Society Review*, Vol.113, No.1, pp.129-161.
- Chaudhri, V. (2003), Executive Compensation: Understanding the Issues, *The Australian Economic Review*, Vol. 36, No.3, pp. 300-305.
- CMA (2002b), Gazette Notice No.3362, May 14, The Capital Markets Act (Cap 485A), Guidelines on Governance practices by Public Listed Companies in Kenya, available at: <http://www.nse.co.ke/download/corporate%20Governance%20Guidelines,%2022002.pdf>
- Combs, J. G. and Skill, M. S. (2003), Managerialist and Human Capital Explanations for Key Executive Pay Premiums: A Contingency Perspective, *The Academy of Management Journal*, Vol.46, No.1, pp. 63-73.
- Conlon, E. and Parks, J. (1988), The effects of monitoring and traditional compensation arrangements: An experiment on principal/agent dyads in F. Hoy (Ed.), *Best paper proceedings*, pp.191-195, Anaheim, CA: Academy of management.
- Crespi-Cladera, R. and Gispert, C. (2003), Total Board Compensation, Governance and Performance of Spanish Listed Companies, *Labour*, Vol. 17, No.1, pp.103-126.
- Defusco, R. A., McLeavy, D.W., Pinto, J. E. and Runkle D. E.(2001), *Quantitative methods for Investment Analysis*, Charlottesville, Virginia CFA Institute

- Duffheus, P., and R. Kabir, (2007), Is the pay-performance relationship always positive – evidence from the Netherlands, *Journal of Multinational Financial Management*, Vol.18, pp.45–60.
- Eichholtz, M. A, Kok, N. and Otten. R. (2008), Executive Compensation in UK Property Companies, *The Journal of Real Estate Finance and Economics*, Vol. 36, No.4, pp. 405-426.
- Fama, E. and Jensen, M. (1983), Separation of ownership and control. *Journal of Law and Economic*, Vol.26, pp. 301-325.
- Fama, E. (1980), Agency problems and the theory of the firm, *Journal of Political Economy*, Vol.88, pp.288-307.
- FCS Group (2005), Best practices and trends in performance based contracting, *Office of financial Management*, Available at: [http://www.ofm.wa.gov/contracts/perf\\_based\\_contracting.pdf](http://www.ofm.wa.gov/contracts/perf_based_contracting.pdf) Last accessed on 31 August 2009.
- Fernandes, N. (2008), EC: Board compensation and firm performance: the role of independent board members, *Journal of Multinational Financial Management*, Vol. 18, pp. 30–44.
- Fischer, S. and Merton, R.C. (1985), Macroeconomics and Finance: The Role of the Stock Market, NBER Working Paper Series, Vol. w1291, available at SSRN: <http://ssrn.com/abstract=304853>.
- FrankfortNachmias, C. and Nachmias (1996) Research methods in the social sciences, 5<sup>th</sup> edition, London, UK Arnold
- Garvey, G. and Swan, P. (1994), The Economics of Corporate Governance: Beyond the Marshallian Firm, *Journal of Corporate Finance*, no. 1, pp. 139-174.
- Gibbons, R. and Waldman, M. (1999), Careers in Organizations: Theory and Evidence, *Handbook of labor economics*, Vol 3B, Amsterdam; New York and Oxford: Elsevier Science, North- Holland, 2373-437.
- Gibbons, R. and Murphy, J. (1990), Relative performance evaluation for chief executive officers, industrial and labour review, *ILR Review*, Corenell University, Vol. 43(3), pp. 30-51.
- Gill, J. and Phil, J. (2002), Research Methods for Managers, 3<sup>rd</sup> Edition, Paul Chapman Ltd., London.
- Gitman, L. (2003), *Principles of managerial finance*, Boston, MA : Addison-Wesley Pub.

- Goering, G. E. and Harikumar, T. (1999), Investment decisions and managerial compensation design in the presence of product market rivalry, *Managerial and Decision Economics*, Vol. 20, No. 2, pp. 87-97.
- Hall, B.J. and Murphy, K.J. (2003), The Trouble with Stock Options, *Journal of Economic Perspectives*, Vol. 17, No.3, pp.49-70.
- Hassan, S., Christopher, T., Evans, R. (2003), Directors' remuneration and firm performance: Malaysian evidence, *Malaysian Accounting Review*, Vol. 2 No.1, pp.57-67.
- Hill, J. G. (2006), *Regulating Executive Remuneration: International Developments in the Post-Scandal Era 2-4* (Sydney Law Sch. Legal Studies Research Paper, Paper No. 06/10, 2006), available at <http://ssrn.com/abstract=922299> last accessed August 10 2009.
- Hogan, T.D. and McPheters, L. R. (1980), Executive Compensation: Performance versus Personal Characteristics, *Southern Economic Journal*, Vol. 46, No. 4, pp. 1060-1068.
- Hoskisson, R. E., Eden, L., Lau, C. M. and Wright, M. (2000), Strategy in emerging economies, *The Academy of Management Journal*, Vol. 43, No. 3, pp. 249-267.
- Hubbard, R.G. and Palia, D. (1994), Executive pay and performance: Evidence from the banking industry, *NBER Working Paper*, No. 4704.
- International Accounting Standards Board, (2009), *International Financial Reporting Standards*, London, IASCF Publications.
- Jensen, M. C. and Murphy, K. J. (1990a), CEO Incentives – It is not How much you pay, but How, *Harvard Business review*, Vol. 68, pp.138- 49.
- Jensen, M.C. and Meckling, W.H. (1976), Theory of the firm: Managerial behavior, agency costs and ownership structure, *Journal of Financial Economics*, Vol. 3, No.4, pp. 305-360.
- Jensen, M.C. and Murphy, K. J. (1990b), Performance Pay and Top-Management Incentives, *The Journal of Political Economy*, Vol. 98, No. 2, pp. 225-264.
- Jensen, M. (1986), Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers, *American Economic Review*, Vol. 76, No.2, pp. 323-29.
- John, K. and Senbet, L. (1998), Corporate Governance and Board Effectiveness, *Journal of Banking and Finance*, No. 22, pp. 371-403.
- Johnson, R.R. and Kubly, P. (2007), *Elementary Statistics*, 10<sup>th</sup> edition Belmont, CA: Thomson/Brooks/Cole.
- Joskow, P.L. and Rose, N.L. (1994), CEO Pay and Firm Performance: Dynamics, Asymmetries and Alternative performance measures, *NBER working paper*, No. 4976

Kaplan, R.S. and Norton, D. P. (1992), The Balanced Scorecard: Measures that Drive Performance, *Harvard Business Review*, (Jan-Feb), pp. 71-79.

Kato, T. and Long, C., (2006), Executive Compensation, Firm Performance, and Corporate Governance in China: Evidence from Firms Listed in the Shanghai and Shenzhen Stock Exchanges, *Economic Development and Cultural Change*, Vol. 54, No.4, pp. 945-83.

Kerin, P. (2003), Executive Compensation: Getting the Mix Right, *The Australian Economic Review*, Vol. 36, No. 3, pp. 324-32.

Kosnik, R. (1987), Greenmail: A study in board performance in corporate governance, *Administrative Science Quarterly*, Vol.32, pp.163 -185.

Kubo. K. (2001), The Determinants of Executive Compensation in Japan and the UK: Agency Hypothesis or Joint Determination Hypothesis?, CEI Working Paper Series, No. 2001- 2 Institute of Economic Research Hitotsubashi University.

Kubo, K. (2005), Executive Compensation Policy and Company Performance in Japan, *Corporate Governance: An International Review*, Vol. 13, No.3, pp.429-436.

Kwama, K. (2009), Do Top CEO's Earn their Pay?, The East African Standard, available at:  
<http://www.eastandard.net/mag/InsidePage.php?id=1144007331&cid=457&> Last accessed 16 August 2009.

Lambert, R.A. and Larcker, D.F. (1987), An analysis of the Use of accounting and Market Measures of Performance in Executive compensation Contracts, *Journal of Accounting research*, Vol.25, pp.85 -125.

Lazear, E. P. and Rosen, S. (1981), Rank-Order Tournaments as Optimum Labor Contracts, *The Journal of Political Economy*, Vol. 89, No. 5, pp. 841-864.

Lee, K. W., Lev, B. and Yeo, G.H.H. (2008), Executive pay dispersion, corporate governance, and firm performance, *Review of Quantitative Finance and Accounting*, Vol. 30, No.3, pp. 315-338.

Main, G. M., Jackson, C. and Pym, J. and Wright, V. (2008), The Remuneration Committee and Strategic Human Resource Management, *Corporate Governance: An International Review*, Vol. 16, No.3, pp. 225-238.

McLaney, E. (2006), *Business finance: theory and practice*, 7th edition - New York : Financial Times/Prentice Hall.

Murphy, K. J. (1997), Executive compensation and the Modern Industrial Revolution, *International Journal of Industrial Organization*, Elsevier, Vol. 15, No.4, pp. 417 – 425.

- Murphy, K. J. (1999), Executive Compensation, *Handbook of Labor Economics. Volume 3b*. Amsterdam; New York and Oxford: Elsevier Science, North-Holland, 2485-563.
- Neuman, W.L. (2006), Social Research Methods Qualitative and Quantitative Methods, 6<sup>th</sup> edition, Person education Inc.
- NSE (2002), *Nairobi Stock Exchange Handbook: An authoritative 5 year handbook of performance results of listed companies*, (2002 edition), Nairobi Stock Exchange, Nairobi.
- NSE (2008), Nairobi Stock Exchange Handbook, (2008 edition) Nairobi Stock Exchange, Nairobi.
- OECD Study (1999), OECD Principles of Corporate Governance, available at: [www.oecd.com](http://www.oecd.com) Last accessed 30.06.2009.
- OEC, Study (2008), Africa Economic Outlook, Available at: <http://www.oecd.org/dataoecd/12/54/40578108.pdf> Last accessed 9 January 2010.
- Ozkan, N. (2007), Do corporate governance mechanisms influence CEO compensation? An empirical investigation of UK companies', *Journal of Multinational Financial Management*, Vol. 17, No. 5, pp. 349-364.
- Pearce, J., Stevenson, W. and Perry, J. (1985), Managerial compensation based on organizational performance: A time series analysis effects of merit pay, *Academy of management Journal*, Vol.28, pp.261 – 278.
- Peng, L. and Röell, A. (2008), Manipulation and Equity-Based Compensation, *American Economic Review*, Vol.98, No.2, pp. 285-290.
- Perrow, C. (1986), Complex Organizations. New York Random House.
- Randhoy, T., and J. Nielsen, (2002) , Company performance, corporate governance and CEO compensation in Norway and Sweden, *Journal of Management and Governance*, Vol. 6, pp. 57–81.
- Rose, N. L. and Wolfram, C. (2002), Regulating Executive Pay: Using the Tax Code to Influence Chief Executive Officer Compensation, *Journal of Labor Economics*, Vol. 20, No. 2, pp.138- 175.
- Rosen, S. (1992), Contracts and the Market for Executives, in Lars Werin and Hans Wijkander (eds), *Contract Economics*, Blackwell Publishers.
- Ross, E. (1973), The economic theory of Agency: The Principals problem, *American Economic Review*, Vo. 63, pp. 134 – 139.
- Ross, S.A, Westerfield, R W. and Jaffe, J. (2008), *Modern financial management*; New York : McGrawHill.

Shah, A.Z.A, Javed, T. and Abbas, M. (2009), Determinants of CEO Compensation *Empirical Evidence from Pakistani Listed Companies*, International Research Journal of Finance and Economics, No. 32, Available at <http://www.eurojournals.com/finance.htm> Last Accessed 20 November 2009.

Shavell, S. (1979), Risk sharing and incentives in the principal and agent relationship. *Bell Journal of economics*, Vol.10, pp. 53 -73.

Shleifer, A. and Vishny, R. W. (1997), A Survey of Corporate Governance, *The Journal of Finance*, Vol. 52, No. 2, pp. 737-783.

Sloan, R. G. (1993), Accounting earnings and Top Executive Compensation, *Journal of Accounting and economics*, Vol.16, pp. 55 -100.

Smith, A. (1776), *The Wealth of Nations*, Edited by Edwin Cannan, 1904. Reprint edition 1937. New York, Modern Library.

Sridharan, U. V. (1996), CEO Influence and Executive Compensation, *The Financial Review*, Vol. 31, No., pp. 51-66.

Ungson, G. and Steers, R. (1984), Motivation and politics in executive compensation, *Academy of Management Review*, Vol. 9, pp. 313-323.

Van Horne, J.C., and Wachowicz, J.M. (2001), *Fundamentals of financial management*, 11<sup>th</sup> edition, Delhi Pearson Education Asia.

Watson, D. and Head, A. (2007), *Corporate finance Principles and practice*, 4th - Harlow, UK Prentice Hall/Financial Times.

Weiss, C.A., (2001), *Introductory statistics*, C.A., 6th edition, Boston Addison-Wesley.

Williamson, O. (1964), *The Economics of Discretionary Behaviour: Managerial Objectives in a Theory of the Firm*, Englewood Cliffs, NJ.: Prentice Hall.

Zeckhauser, R. and Pound, J. (1990). "Are large shareholders effective monitors? An investigation of share ownership and corporate performance", (in R. Hubbard (ed), *Asymmetric Information, Corporate Finance and Investment*), University of Chicago Press.

## APPENDICES

### APPENDIX ONE: Companies under Study

| <b>(i) Agricultural sector</b>           |                                 | <b>Nature of business</b>                 |
|------------------------------------------|---------------------------------|-------------------------------------------|
| 1                                        | Kakuzi                          | Coffee, tea, and fruits                   |
| 2                                        | Rea Vipingo Sisal Estate        | Sisal                                     |
| 3                                        | Sasini Tea and Coffee           | Tea and coffee                            |
| <b>(ii) Commercial and Services</b>      |                                 |                                           |
| 4                                        | Car & General Kenya             | Tyre retreads and machinery               |
| 5                                        | CMC Holdings                    | Motor vehicles distribution               |
| 6                                        | Kenya Airways                   | Airline                                   |
| 7                                        | Marshalls East Africa           | Motor vehicles                            |
| 8                                        | Nation Media Group              | Newspaper, radio, television and courier  |
| 9                                        | Standard Group                  | Newspaper, radio and television           |
| 10                                       | TPS Serena                      | Tours Promotion Services; hotels          |
| <b>(iii) Industrial and allied</b>       |                                 |                                           |
| 11                                       | Athi River Mining               | Cement, fertilizers, minerals             |
| 12                                       | Bamburi Cement                  | Cement                                    |
| 13                                       | BOC Kenya                       | East African Oxygen                       |
| 14                                       | British American Tobacco        | Cigarette                                 |
| 15                                       | Crown-Berger (Kenya)            | Paints                                    |
| 16                                       | Mumias Sugar                    | Sugar processing                          |
| 17                                       | EA Portland Cement              | Cement                                    |
| 18                                       | East African Breweries          | Beer                                      |
| 19                                       | Kenya Power and Lighting        | Electricity Supply                        |
| 20                                       | Kenya Oil                       | Petroleum                                 |
| 21                                       | East African Cables             | Cable Manufacture                         |
| 22                                       | Sameer Group                    | Agribusiness, manufacturing and transport |
| 23                                       | Total Kenya                     | Petroleum                                 |
| 24                                       | Unga Group                      | Flour milling                             |
| <b>(iv) Finance and Investments</b>      |                                 |                                           |
| 25                                       | Barclays Bank of Kenya          | Banking and Investment                    |
| 26                                       | Centum Investment Company       | Investment                                |
| 27                                       | Diamond Trust Bank of Kenya     | Banking                                   |
| 28                                       | Housing Finance Company         | Banking and Mortgage finance              |
| 29                                       | Jubilee Insurance               | Insurance                                 |
| 30                                       | Kenya Commercial Bank           | Banking                                   |
| 31                                       | National Bank of Kenya          | Banking                                   |
| 32                                       | National Industrial Credit Bank | Banking                                   |
| 33                                       | Pan Africa Insurance            | Insurance                                 |
| 34                                       | Standard Chartered Bank         | Banking                                   |
| <b>(B) ALTERNATIVE INVESTMENT MARKET</b> |                                 |                                           |
| 35                                       | Express Kenya                   | Logistics                                 |
| 36                                       | Kapchorua Tea                   | Tea                                       |
| 37                                       | Williamson Tea Kenya            | Tea                                       |

## **APPENDIX TWO: Letter of Introduction**

STRATHMORE UNIVERSITY

15 October 2009

Dear Sir/Madam,

### **REF: RESEARCH ON FIRM PERFORMANCE AND EXECUTIVE PAY**

I am a second year student in the Faculty of Commerce at Strathmore University pursuing Masters in Commerce (Finance option). I am conducting a study under the supervision of Dr X. N. Iraki looking at the relationship between executive compensation and firm performance for Nairobi Stock Exchange Companies. Your company is among the ones selected for study.

I would appreciate if you would complete the attached brief questionnaire. Completion of the questionnaire is expected to take about 10 to 15 minutes of your time. There are no known or anticipated risks to participation in this study. Participation in this study is voluntary and anonymous. Further, all information you provide will be considered confidential.

If after receiving this letter, you have any questions about this study, or would like additional information to assist you in reaching a decision about participation, please feel free to contact the researcher on 0722 292195 or Strathmore University (School of Graduate Studies on 606155)

Thank you in advance for your interest in this study.

Yours sincerely,

**Geoffrey Injeni**

## APPENDIX THREE: Questionnaire

# STRATHMORE UNIVERSITY

## FACULTY OF COMMERCE

### FORMS OF DIRECTORS' REMUNERATION

#### INTRODUCTION

The purpose of this questionnaire is to assist in getting information from the remuneration committee or other officers of the company, the main forms of directors' remuneration and the important factors that determine directors' remuneration. Any information provided will be held in strict confidence.

Thank you in advance for your cooperation.

#### **Section A: General Information**

1. Name of the firm (Optional) \_\_\_\_\_

\_\_\_\_\_

2. Sector or Industry of Operation (Tick as appropriate)

- ☐ Agricultural
- ☐ Banking
- ☐ Commercial
- ☐ Manufacturing
- ☐ Others \_\_\_\_\_

3. Is the company locally or foreign owned?

- ☐ Both locally and foreign owned
- ☐ Local ownership
- ☐ Foreign Ownership

**Section B: Forms of directors' remuneration**

4. Does the company pay the following to directors?

|                                    | Yes                      | No                       |
|------------------------------------|--------------------------|--------------------------|
| Basic salary and benefits          | <input type="checkbox"/> | <input type="checkbox"/> |
| Short-term benefits – bonus        | <input type="checkbox"/> | <input type="checkbox"/> |
| Long-term benefits – Stock options | <input type="checkbox"/> | <input type="checkbox"/> |
| Entry benefits – golden hello      | <input type="checkbox"/> | <input type="checkbox"/> |
| Exit benefits – golden bye bye     | <input type="checkbox"/> | <input type="checkbox"/> |
| Others_____                        |                          |                          |

---

**Section C: Factors that determine directors' remuneration**

5. Are the following factors considered by the company when determining directors' remuneration?

|                                          | Yes                      | No                       |
|------------------------------------------|--------------------------|--------------------------|
| Qualifications (Academic & professional) | <input type="checkbox"/> | <input type="checkbox"/> |
| Experience                               | <input type="checkbox"/> | <input type="checkbox"/> |
| Age                                      | <input type="checkbox"/> | <input type="checkbox"/> |
| Firm performance                         | <input type="checkbox"/> | <input type="checkbox"/> |
| Tax                                      | <input type="checkbox"/> | <input type="checkbox"/> |
| Others_____                              |                          |                          |

---

6. Which of the factor(s) given in 5 above are considered to be important in determining director's emoluments? (If there are several, then rank them in order of importance).

---

Others comments and suggestions

---

---

**THANK YOU FOR TAKING YOUR TIME TO FILL THIS  
QUESTIONNAIRE. YOUR RESPONSE IS HIGHLY APPRECIATED.**