THE RELATIONSHIP BETWEEN BOARD REMUNERATION AND FINANCIAL PERFORMANCE AMONG LISTED FINANCIAL SERVICES COMPANIES IN KENYA

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“You get the board you pay for”. This means that to attract, retain the best directors, the board must offer attractive packages.

However, corporate governance failures and corporate collapses have increased concern over the increasing levels of board remuneration.

The 2008-09 financial crisis raised serious questions about the role of Corporate Governance mechanisms in determining remuneration and incentive systems.

High levels of director’s remuneration may be caused by greed in executive management or weak governance by shareholders.

In collusion with management, directors can also turn a blind eye to accounting irregularities and corporate losses, which threaten the long term growth and survival of the company.

With conflicting findings in empirical literature, recent cases of corporate governance failures in Kenya, and the paucity of research on the phenomenon in Kenya, there was a need to investigate the relationship between board remuneration and financial performance.
PURPOSE OF THE STUDY

- To investigate the relationship between Board Remuneration and Financial Performance among listed financial services companies in Kenya.

- Research Question:
  What is the effect of board remuneration on the financial performance of listed financial services companies in Kenya?
The study is grounded in the agency theory.

This is a contractual relationship where the principal engages the agent to perform a service.

It is the expectation that the agent will act in the principal’s best interest.

However, the agent may exhibit opportunistic behaviour, hence the need to control the agency problem.

The board of directors are representatives of shareholders (principal) and are appointed to maximize shareholder returns and monitor/oversight the executive management (agent) to safeguard against opportunistic behaviour.
<table>
<thead>
<tr>
<th>Authors</th>
<th>Title</th>
<th>Objectives</th>
<th>Methodology</th>
<th>Results</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>No significant relationship between FP and ROE and Tobin’s Q.</td>
<td>- No significant relationship between board remuneration and EAT.</td>
</tr>
<tr>
<td>Muller (2014)</td>
<td>Do corporate board compensation characteristics influence the FP of listed companies?</td>
<td>Investigates the effect of compensation characteristics on FP.</td>
<td>Sample: FTSE100, London Stock Exchange, 2010-2011 Variables: BR &amp; FP (ROA and ROE). Data analysis: OLS Reg.</td>
<td>- Significant relationship between board remuneration, ROA and ROE.</td>
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</table>
| Barontini & Bozzi (2009)      | Board compensation and ownership structure: empirical evidence for Italian listed companies | Investigates the relationship between Board remuneration and performance | Sample: Listed firms at Milan Stock Exchange  
Data: 1995-2002  
Data analysis: Regression | - Significant relationship bt BR and corporate ownership controlling shareholder agreements  
- BR associated with firm performance |
IRRC to measure stock incentives  
Data analysis: Regression | Stock option incentives are –vely associated with meeting/beating earnings  
- Independent directors manipulating option-based incentives |
Sample: 428 companies, Malaysia.  
Variables: board remuneration and FP.  
Data analysis: Reg. | -No significant relationship between BR & FP  
- Significant relationship bt BR and EPS & ROE & CEO pay and performance |
METHODOLOGY

- A cross sectional survey design was used in the study.
- Audited annual financial statements were obtained from NSE and CMA for the board remuneration and financial performance.
- Statistical Packages for Social Sciences (SPSS Version 21) was used for data analysis.
- Pooled cross-sectional time-series data analysis was done using the mixed procedure to estimate the relationship between BR & FP.
- The linear regression model applied took the form of:
  \[ Y = \beta_0 + \beta_1 BR + \varepsilon \]

  Where:  
  - \( Y = \)FP measured as ROA, ROE, DY, and EPS
  - \( BR = \) Board Remuneration
  - \( \varepsilon = \) Error term
  - \( \beta_1 = \) slope of the regression equation

- The coefficient of determination - strength of the relationship
- Standardized coefficients - comparative explanatory power, direction and significance of the explanatory variables in the regression model.
RESEARCH FINDINGS AND DISCUSSIONS

Descriptive Statistics

- Significant variations on the level of the variables between companies

Table 1: Descriptive statistics for variables

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>BR</td>
<td>110</td>
<td>1.1</td>
<td>102.0</td>
<td>10.142</td>
<td>15.1396</td>
</tr>
<tr>
<td>ROA</td>
<td>110</td>
<td>-1.97</td>
<td>18.63</td>
<td>3.2565</td>
<td>2.78669</td>
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<tr>
<td>ROE</td>
<td>110</td>
<td>-16.26</td>
<td>49.82</td>
<td>17.7545</td>
<td>10.65722</td>
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<tr>
<td>DY</td>
<td>110</td>
<td>.00</td>
<td>11.15</td>
<td>3.1730</td>
<td>2.48986</td>
</tr>
<tr>
<td>EPS</td>
<td>110</td>
<td>-13.63</td>
<td>37.00</td>
<td>5.5310</td>
<td>6.69586</td>
</tr>
<tr>
<td>Valid N (list wise)</td>
<td>110</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- Trend analysis shows - steady increase in BR from Kshs 4.6M (2003) - Kshs 22.23M (2013) Figure 1: Board Remuneration
Regression Analysis

- Overall findings show significant relationship - BR & DY (p=0.006) in the financial services industry
- Relationship – BR & ROA(p=0.830), ROE (p=0.061) & EPS (p=0.216) was not significant at the industry level

Table 3: Regression Coefficients BR & FP in the Industry

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROA</td>
<td>(Constant)</td>
<td>3.295</td>
<td>.322</td>
<td>10.244</td>
</tr>
<tr>
<td></td>
<td>Board Remuneration</td>
<td>-.004</td>
<td>.018</td>
<td>-.215</td>
</tr>
<tr>
<td>ROE</td>
<td>(Constant)</td>
<td>16.477</td>
<td>1.211</td>
<td>13.611</td>
</tr>
<tr>
<td></td>
<td>Board Remuneration</td>
<td>.126</td>
<td>.067</td>
<td>.179</td>
</tr>
<tr>
<td>DY</td>
<td>(Constant)</td>
<td>2.691</td>
<td>.296</td>
<td>9.096</td>
</tr>
<tr>
<td></td>
<td>Board Remuneration</td>
<td>.054</td>
<td>.019</td>
<td>.273</td>
</tr>
<tr>
<td>EPS</td>
<td>(Constant)</td>
<td>6.124</td>
<td>.820</td>
<td>7.464</td>
</tr>
<tr>
<td></td>
<td>Board Remuneration</td>
<td>-.066</td>
<td>.053</td>
<td>-.125</td>
</tr>
</tbody>
</table>
ROA & ROE are indicators of the efficiency, while EPS demonstrates market performance and DY is a measure of shareholder returns. All these are measures of financial performance.

The study demonstrates a positive and significant relationship between BR and DY, but not a significant relationship with ROA, ROE, and EPS.

Study agrees with Miyaenda, Oirere, & Miyogo (2012), who reported no relationship between board remuneration and ROE and Tobin’s Q.

Study also agrees with other researchers that reported inconclusive results - BR & FP - Duffhues & Kabir (2008) and Conyon & Schwalbac (2000). Findings show inconclusive evidence since BR is only positively related to DY, and not to ROA, ROE, and EPS.

The positive and significant relationship shows that directors are effectively performing their role of maximizing shareholder wealth, control agency behaviour and serve as a disciplining and monitoring mechanism used by the board to reduce the agency costs of equity.

Since dividends are crucial in institutional frameworks where governance provisions are unfavorable for shareholders Haye (2013), the study suggests that Kenya’s corporate governance framework is weak and do not offer adequate protection to shareholders.
CONCLUSIONS & RECOMMENDATIONS

- The study concludes that there is a positive and significant relationship between board remuneration and dividend yield. However, similar results were not reported for ROA, ROE, and EPS.

- Dividend payout is a measure of shareholder returns, and can be used to control agent behaviour, as postulated in agency theory.

- The board of director’s is performing its role of maximizing shareholder returns even though the country’s corporate governance framework does not offer adequate protection to shareholders.

- The study recommends that financial services companies can rely on market data to establish the best mix of fixed and variable remuneration options (director’s fees and allowances, attendance fees, cash equity, or company equity), since directors are committed to maximizing shareholder returns.
THANK YOU