

# THE LINK BETWEEN COMPLIANCE WITH CORPORATE GOVERNANCE DISCLOSURE CODE, AND FIRM PERFORMANCE FOR KENYAN FIRMS.

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## Abstract

In 2002, The Capital Markets Authority (CMA) of Kenya issued the CMA guideline on Corporate Governance. Listed Companies are required to comply or give reasons for non-compliance with the “guideline”. Recent empirical work in developed markets investigating the link between compliance and performance of companies has documented weak or non-existent relationship. Furthermore the direction of causality of any relationship is debatable. Despite the prominence of the issue, academics and practitioners in developing markets have been niggardly in devoting commensurate efforts and attention on this issue with the result that few if any studies exist. We investigate the extent to which differences in the extent of firm level corporate governance reporting help to explain firm performance in a cross-section of companies listed at the Nairobi Stock Exchange. Constructing a broad Kenyan corporate governance index (KCGI) for Kenyan public firms, we document a positive relationship between governance practices and firm performance. This has implications for investing community if an investment strategy that bought high-KCGI firms and shorted low-KCGI firms would earn significant abnormal returns.

**Key words:** *Corporate governance, Corporate governance index, Firm performance,*

## 1. INTRODUCTION

Corporations have become the preferred way of organizing productive activities in most countries. Yet one feature of corporations is both its strength and its Achilles heel at the same time. This is the divorce of control from ownership. In a corporation the separation, facilitates the corporation to be run professionally. Yet this separation is the genesis of the agency conflicts that bedevil the corporate form. Proper corporate governance has been touted as the panacea that mitigates the agency conflicts, achieving a level of convergence in the inherently divergent of interests of management and shareholders.

Cognizant of the need to enhance the good governance of corporation, a host of global initiatives have been mooted to provide governance principles for the effective management and control of these organizations. Most of the initiatives have featured the developed economies like the UK, the US, Canada, France, and Germany. However developing countries are not far behind as witnessed by the recent proliferation of “Codes of Best Practice” from South Africa, Nigeria, and Brazil etc.

Corporate governance defined by the organization for Economic Co-operation and Development (OECD) as the processes by which corporate entities, particularly public

liability companies, are directed and controlled has become a topical issue in many countries. The debate on the role and control of corporations has moved to the top of many national agendas as a result of the spread of US-style shareholder activism, privatizations and the opening-up of markets in the developing countries, financial crises and market crashes, as well as the growing incidence of bad corporate management and outright fraud.

Academic researchers, practitioners, and regulators have come to recognize the importance of good corporate governance - a vigilant board of directors, timely and adequate disclosure of financial information, meaningful disclosure about the corporation, and transparent ownership - in enhancing the well-being of the corporate sector. At the national level, promotion of good corporate governance practice improves the ability of domestic firms to attract more investment from the international investment community.

Internationally, the Asian financial crisis of 1997, and the more recent the Enron and Parmalatt crises underscored the importance of structural reforms in the governance of the business sector. Since then, various initiatives have been undertaken to promote such reforms. The international investment community has developed several indices to measure the state of corporate governance. For example, Standard and Poor's Transparency and Disclosure Index assesses the transparency and disclosure practices of corporations around the world, while the Crédit Lyonnais Corporate Governance Index applies some major corporate governance factors - including discipline, transparency, independence, accountability, responsibility, fairness, and social awareness - to rate corporations in different markets. In East Asia, in 2001, ministers of the Asia-Pacific Economic Cooperation countries endorsed guidelines for good corporate governance practices as set out by the Pacific Economic Cooperation Council (PECC).

Corporate governance refers in essence to the organization of the relationship between owners and managers of a corporation. The term corporate governance has two components: corporate, which refers to corporations or big companies; and governance, which is defined as the act, fact, or manner of governing. The term was defined by the Cadbury Committee, a group set up in the UK in 1991 to examine standards of financial reporting and accountability, as 'the system by which companies are directed and controlled'.

Lanno (1999), defines corporate governance as the organization of the relationship between the owners and the managers in the control of a corporation. He goes on to add that a good corporate governance system will be able to tackle the conflicts of interest between managers and owners of a corporation, and resolve them. Although other stakeholders, such as the workforce, government agencies, banks, suppliers and customers, or the public at large, have an interest in corporate control, ultimately, it is the shareholder-manager relationship which is the most essential in corporate governance and which best lends itself to international comparison. It should be noted, however, that in some countries where there is lesser shareholder participation, other 'stakeholders'

have been given greater say in management. In several European countries, employees have seats on the management board, effectively the supervisory board.

More relevantly, in Kenya, The Centre for Corporate Governance defines corporate governance as the manner in which the power of and over a corporation is exercised in the stewardship of its assets and resources so as to increase and sustain shareholder value as well as satisfying the needs and interests of all stakeholders.

The governance of a successful corporation typically includes an effective board of directors that carries out its responsibilities with integrity and competence. An effective board must put in place systems to ensure that the organization obligations to its shareholders are met. They must ensure full and timely disclosure of performance of the business to its owners and the investments community at large (Colley et al 2005).

In recent times, the frontiers of corporate governance have been expanding rapidly, in tandem with the increasing gravity of governance challenges to directors, boards, investors, management, regulators and academicians. Yet issues of governance are not new. Corporate governance has been practiced for as long as there have been corporate entities, characterized by the separation of ownership from management and control. Indeed, Adam Smith shows that he understood the issue of corporate governance, even though he did not use the phrase:

*“Directors of companies, being managers of other people’s money, it cannot well be expected that they will watch over it with the same anxious vigilance with which partners in a corporate company watch over their own”* (Smith 1776 edn 1976; p264).

It was not however until the 1980’s that the topic received much attention.

“The proper governance of companies will become crucial to the world economy as the proper governing of countries”. (Bowes, 2000: p.1).

A decade earlier Peter Drucker, when examining the challenges managers would face in the 1990’s predicted that: “The governance of business is likely to become an issue throughout the developed world”. (The Economist, 21<sup>st</sup> October 1989: p26).

These predictions have come to pass as evidenced by the interest that the subject of corporate governance has generated in the media, professional, academic literature and society at large. Several reasons can be advanced for this interest in corporate governance.

Firstly, the interdependence between the society and business demand that companies be accountable to the society as company decisions have far reaching effects on the society and the environment. Companies not only provide essential goods and services, they pay taxes, create employment and engage in community-based activities and have thus become development partners with the society. As society becomes increasingly dependent on companies it (society) becomes more concerned with corporate activities and their governance as they (companies) play a key role in the creation of wealth both at

the national and the corporate level. Drucker (1974) says that society will scrutinize company activities and especially those of large and visible business so as to ensure accountability.

Secondly, public attention following high profile corporate scandals and collapses in recent times of companies such as Enron, Parmalatt, WorldCom, the Bank of Credit and Commerce International (BCCI), among others, without any warning wiped out the wealth of shareholders in one fell swoop, resulting in intense pressure to reexamine the governance of corporations. Kenya has had its fare share of financial scams as demonstrated by the collapse of Lonrho, Trust Bank, Euro Bank, Kenya Finance Trust and Uchumi Supermarkets Limited. Many scholars ascribe corporate failure to a weak board, unable to exercise their mandate adequately (Stiles (1993).

Thirdly, the hard economic times and shocks all over the world have exposed corporate weaknesses. The volatility of the world economy has significantly increased the risks faced by companies today. Stiles (1993) asserts that in such a non-compromising environment we can no longer afford to overlook corporate fraud, mismanagement and unjustified executive pay awards among other irregularities ((See also Demb and Neubauer;(1992); Dimsdale and Prevezer; (1994)).

Finally, the globalization of economies and the growth of financial and investment markets in the 1990s has presented an opportunity for institutional investors to deploy their massive funds internationally. As they seek to do so, they are insisting on high standards of corporate governance in the companies in which they must invest. (CACG; 1999). Investor confidence can only be enhanced with good corporate practices where there is accountability and transparency. After all, an investor can only trust management once the objectives and the return on their equity has been stated hence the demand for accountability from the directors.

Consequently governments and boards of corporations have been forced to pay attention to fundamental issues of corporate governance as essential for public economic interest. Without investment, companies will stagnate and collapse. If business enterprises do not prosper, there will be no economic growth, no employment, no taxes paid and invariably the country will not develop. The country needs well-governed and managed business enterprises that can attract investments, create jobs and wealth, and remain viable, sustainable and competitive in the global market place.

*“Good corporate governance therefore becomes a prerequisite for national economic development”* (CACG; 1999).

In Kenya, the institutions that have been at the forefront in sensitizing the corporate sector in Kenya on corporate governance are The Capital Markets Authority (CMA), the Nairobi Stock Exchange (NSE), the Center for Corporate Governance (CCG) and Central Bank of Kenya (CBK) which regulates the banking industry.

The CMA created a major impact in the development of corporate governance guidelines in Kenya when it issued in 2002 the Capital Market guidelines on Corporate Governance

Practices and disclosures. These guidelines were published under a gazette notice No. 369 of 25<sup>th</sup> January 2002 and not a legal notice and therefore do not have the force of law. However, certain of the guidelines have subsequently been incorporated into legal notice No.60 of 3<sup>rd</sup> May 2002 as part of the Capital Markets guidelines and are enforceable in law. The stated objective of the CMA guidelines on Corporate Governance is to strengthen and promote the standards of self-regulation and bring the level of governance practices in line with international trends.

Following the CMA guidelines, the NSE amended its Listing Manual and incorporated the CMA guidelines on corporate governance into the continuous obligations of listed companies and it continuously monitors compliance by listed companies with these obligations. In Kenya the emphasis on good corporate governance and accountability to shareholders and stakeholders has been on listed companies. The potential for listed companies being subjected to sanctions for non-compliance by either the CMA or NSE has played an important role encouraging compliance with the guidelines.

The Institute of Certified Public Accountants (Kenya) requires its members to report on the corporate governance practices of companies they audit and the Institute of Certified Public Secretaries (Kenya) also encourage its members to ensure compliance with the corporate governance guidelines. Both institutions train their members on corporate governance issues.

Despite the plethora of initiatives from diverse quarter pushing the Corporate Governance agenda Kenyan, studies on corporate governance have restricted themselves to surveys of the state of compliance with, and determinants of, selected governance mechanisms in various sectors: A sample of the studies include Jebet (2001) documenting the corporate governance structures in listed companies; Kitonga (2002) who studied the need for corporate governance audit in Kenya; Mwangi (2002), surveyed the corporate governance practices in the insurance industry; Mwangi (2003) investigating the determinants of corporate governance practices; and Wambua (2003) who documented the actions taken by boards of companies facing rapid performance declines. In a recent study Mululu (2005) found that board activity is related to a number of corporate governance variables such as the board size, the number of executive directors, number of shares held by the largest shareholder, and that boards increase the frequency of their meetings during financial crises. More recently, Kerich (2007) reports that good corporate governance structures are an important catalyst of the speed with which boards mount successful turn-round strategies in case of performance declines.

The current study will be in the genre of Gompers, Ishi, and Metrick (2003) (hereafter GIM), Black et al. (2005), Padgett and Shabbir (2005), and Silveira et al. (2007), studies which take a holistic approach to corporate governance, construct Indices/Scorecards and test whether a governance premium on the value of companies, and their profitability attaches to sound corporate governance. The researcher is not aware of any effort in Kenya that has approached the issue from this perspective. The objectives of this study were:

1. Construct Corporate Governance Index (CGI) for companies listed at the NSE based on guidelines issued by the Capital Markets Authority..
2. Establish a link between Corporate Governance Index and Performance of listed companies

## **2: LITERATURE REVIEW**

### **2.1 History of corporate governance**

The concept of Corporate Governance has a long history Tricker (2000). In the ancient times, when humans roamed on this earth in tribes, there were tribal communes in existence. The activities of the tribe as well as individual members were supervised by tribal communes to ensure adherence to tribal norms. Over a period of time, the tribal form gave rise to agrarian communities where the concept of family took hold. The family had a structure based on age and experience and the activities of the family members were viewed by the family councils.

In the Roman Empire, specific corporate bodies, such municipal bodies were developed to manage public affairs with transparency for common good. In the Middle East, the nomadic tribes had their councils to ensure fair play and justice. The evolution of Christianity and Islam in the Middle East placed the responsibility of governance on religions. The Church and the Mullahs were the torchbearers of the concept and practice of governance.

In ancient India, the ruling emperors decided the concept and practice of governance. The treaties on economic administration, Arthashastra, written roughly 315 years before Christ developed a complete structure of governance in a kingdom with clear demarcation of authority, responsibility and accountability. In the Far East, Japan and China also placed the governance in the hands of their kings.

In the post Christ period, with improved navigation and availability of vessels, the traders from Europe, especially the Portuguese and the Dutch explored the known expanse of the earth and gave rise to global trading entities. These entities reported to the kings. This was the beginning of corporate governance. As we approach the 16<sup>th</sup> century, the most powerful trading nation, England, formed a variety of regulations and regulatory authorities such as joint stock companies and Bank of England to govern all trading activities on a platform of accountability, efficiency, effectiveness and stakeholders' satisfaction. The concept of corporate governance was the basic platform for these regulations and regulatory authorities and over a period of time the concept and its practice took a firm root for all activities. Commonwealth association for corporate governance defines corporate governance as a defined and promulgated interaction between the directors and management in pursuit of sustained wealth creation for the shareholders and stakeholders.

The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company

objectives are set, and the means of attaining those objectives and monitoring performance (OECD).

Capital Markets Authority (2003) refers to corporate governance as the manner in which the corporation's total portfolio of assets and resources are managed with the objective of maintaining and, increasing shareholders long term value while taking into account the interests of other stakeholders. Thus corporate governance seeks to ensure that the Board of Directors and management act in the best interests of the corporation and its stakeholders.

It is often alleged that boards of directors are more independent as proportion of outside directors increases (John and Senbet (1998). However, Foserg (1989) find no relation between the proportion of outside directors and various performance measures (i.e. sales, return on equity and expenses). Bhagat and Black (2002) find no linkage between the proportion of outside directors and return on assets, asset turnover and stock returns. In contrast, Baysinger and Butler (1985) and Rosenstein and Wyatt (1990) show that the market rewards firms for appointing outside directors. Brickley, Coles and Terry (1994) find a positive relation between proportion of outside directors and stock market reaction to poison pills adoption and Anderson, Mansi and Reeb (2004) show that the cost of debt as proxied by bond yield spreads is inversely related to board independence.

Several studies have examined the separation of CEO and chairman, positing that the agency problems are higher when the same person holds those positions. Using a sample of 452 firms in the Forbes magazines rankings of the 500 largest US public firms between 1984 and 1991, Yermack (1996) shows that the firms are more valuable when the CEO and board chairman are separate. Core, Holthausen and Larcker (1999) find that CEO compensation is lower when the CEO and chairman are separate.

### **2.1.2 Importance of corporate governance**

Corporate governance is concerned with direction and control of corporate bodies. These activities are far more basic as compared to profitability and performance of companies. They lay the foundation for future progress of business. Corporate governance is the framework that ensures accountability. Once it is in place, firms are free to go about their way in creating shareholder value and registering growth.

In less developed countries, corporate governance is a prerequisite for capital market development. New investors can be encouraged to invest in corporate securities only when there is credible corporate governance in force. Without it, investors will not come forward to stake their money in companies and private limited companies will not come forward to list their shares on stock exchanges.

It is sometimes argued that corporate governance mechanism is an alternative to competitive markets. The implication is that competition in product and capital markets can make up for deficiencies in corporate governance. This is a wrong notion. Markets may take time to react; they can be deliberately misled and their corrective action may be very drastic. Past evidence shows that efficient, developed markets do not guarantee good governance. It is better to view governance as assistance to competition; good

governance speeds up competitive adaptation and bad governance slows it down. So whether markets are developed or undeveloped, corporate governance remains a priority area.

The Global Corporate Governance Forum notes ‘Corporate governance has become an issue of worldwide importance. The corporation has a vital role to play in promoting economic development and social progress. It is the engine of growth internationally, and increasingly responsible for providing employment, public and private services, goods and infrastructure. The efficiency and accountability of the corporation is now a matter of both private and public interest, and governance has, thereby, come to the head of the international agenda’

Corporate governance lays down the framework for creating long-term trust between companies and external providers of capital. It improves strategic thinking at the top by inducting independent directors who bring a wealth of experience, and a host of new ideas. Corporate governance limits the liability of top management and monitoring of risk that a firm faces globally. It has long term reputational effects among key stakeholders, both internally (employees) and externally (clients, communities, political/regulatory agents).

A country’s capacity to achieve sustainable prosperity which is progressive economic growth and social development over a prolonged period of time depends on decisions about the allocation, utilization and investments of resources. In the liberalized global market, a country’s capacity to create and produce wealth is closely related to the process by which corporate resources are allocated, utilized or invested. Strategic decisions about the allocation and utilization of corporate resources are the foundations of investments in productive capacities that can make innovation and economic development possible. These decisions are made by or await the judgment of the boards of corporations.

Corporate competitiveness depends on the ability of boards to apply focused intelligence to generate innovative ideas, acquire and apply the knowledge and know how to push and integrate their corporation into the competitive global market (CCG Kenya, 2006).

The positive effect of good corporate governance on different stakeholders ultimately is a strengthened economy, and hence good corporate governance is a tool for socio-economic development. After East Asian economies collapsed in the late 20<sup>th</sup> century, the World Bank’s president warned those countries, that for sustainable development, corporate governance has to be good. Economic health of a nation depends substantially on how sound and ethical businesses are.

## **2.2 Theories of Corporate Governance**

### **Agency theory**

The agency relationship is described in the work of Jensen and Meckling (1976). The agency theory identifies the agency relationship where one party, the principal (The Company), delegates work to another party, the agent (Board of Directors).

In the context of corporations and issues of corporate control, agency theory views Corporate Governance mechanisms as being an essential monitoring device in ensuring



that any problems that may be brought about by principal-agent relationships are minimized.

#### **Transaction Cost Economics**

Transaction cost economics (TCE) as expounded by the work of Williamson (1975, 1984) is often viewed as closely related to agency theory. TCE views the firm as governance structure whereas agency theory views the firm as a nexus of contrasts. As firms grow in size, as may be caused by desire to achieve economies of scale amongst other factors, there is an increasing need for more capital which needs to be raised from the capital markets and thus possibility of widening the shareholder base.

#### **Stakeholder Theory**

The stakeholder theory takes account of a wider group of constituents rather than focusing on shareholders. A consequence of focusing on shareholders is maintenance of shareholder value as paramount, whereas when a wider stakeholders group such as employees, providers of credit, customers, suppliers, government and local authority is taken into account the overriding focus on shareholder value becomes less evident. This means that the shareholders have a vested interest in trying to ensure that the resources are used to maximum effect which in turn should be to benefit the society as a whole.

#### **The Stewardship Model**

In the stewardship model 'managers are good stewards of the corporations and diligently work to attain high levels of corporate profit and shareholder returns' (Donaldson & Davis 1991). Donaldson & Davis note that 'Managers are motivated by achievement and responsibility needs' and given the needs of managers for responsible, self-directed work, organizations may be better served to free managers from being submissive to non-executive director dominated Boards'.

#### **Class Hegemony Theory**

Hegemony is defined as the process by which the dominant classes or class fractions, through their privileged positions propagate values that reinforce their control over politics and the economy. These values form a dominant ideology. The dominant ideology in any society is a set of common sense assumptions that legitimates the existing distribution of power. Ideology makes this structure of power seem 'natural', 'normal' or 'inevitable' and therefore beyond challenge.

Class hegemony in the case of Corporate Governance could include the shareholder ship of corporate entity, or other stakeholder ship. It would therefore imply that there is a grouping of shareholders who would be seen as more superior to others and hence their views are considered more valuable than the ideas of the rest of the shareholder/stakeholders.

#### **Managerial Hegemony Theory**

It can be argued that management of any company would have the superior knowledge of the details of business in a certain industry, and thus are best suited to direct the corporation in what would be perceived as the best path for the company.

### **2.3 Corporate Governance Principles**

The concept of corporate governance embodies a number of accepted management tools which have been around for some time. The value of corporate governance is that it draws these tools together into a logical, interrelated set of principles. Key elements of good corporate governance principles include honesty, trust and integrity, openness, performance orientation, responsibility and accountability, strategy and value, mutual respect, corporate compliance and communication, and commitment to the organization.

Of importance is how directors and management develop a model of governance that aligns the values of the corporate participants and then evaluate this model periodically for its effectiveness. In particular, senior executives should conduct themselves honestly and ethically, especially concerning actual or apparent conflicts of interest, and disclosure in financial reports.

Commonly accepted principles of corporate governance include:

- **Shareholder Rights and equitable treatment of shareholders**

Organization should respect the rights of shareholders and help shareholders to exercise those rights. They can help shareholders exercise their rights by effectively communicating information that is understandable and accessible and encouraging shareholders to participate in general meetings.

- **Interests of other stakeholders**

Organizations should recognize that they have legal and other obligations to all legitimate stakeholders.

- **Role and responsibilities of the board**

The board needs a range of skills and understanding to be able to deal with various business issues and have the ability to review and challenge management performance. It needs to be of sufficient size and have an appropriate level of commitment to fulfill its responsibilities and duties. There are issues about the appropriate mix of executive and non-executive directors. The key roles of chairperson and CEO should not be held by the same person.

- **Integrity and ethical behavior**

Organizations should develop a code of conduct for their directors and executives that promotes ethical and responsible decision making.

- **Disclosure and transparency**

Organizations should clarify and make publicly known the roles and responsibilities of board and management to provide shareholders with a level of accountability. They should also implement procedures to independently verify and safeguard the integrity of the company's financial reporting. Disclosure of material matters concerning the organization should be timely and balanced to ensure that all investors have access to clear, factual information.

### **2.4 CMA Corporate Governance Guidelines**

To explain the role of board activity in corporate governance we relied on the notion (advanced by Vafeas (1999), and Weir et al (2002)) that governance mechanisms are substitutes or complements, their levels being determined by each firm's broader control

environment. It should also be recognized that not all board activity will be productive because routine tasks and inefficiencies consume some time. We define below the governance mechanisms (board characteristics) which may, by and large, determine board activity and how they were measured.

**Board Meetings:** Neither the Companies Act nor the CMA guidelines on corporate governance prescribe the frequency of the board meetings. However, a number of public listed companies in Kenya now report on the number of board meetings they held in the year.

In this study the main variable of interest which is used as a proxy for the intensity of board activity is the number of meetings (excluding telephonic meetings of the board) held by the board of directors as recorded in the firms' minute books. I assumed that the characteristics of the meetings for example content, quality, location, length, and the level of interaction at the meeting will hold constant during the period of the study.

**Board Size:** The Companies Act is silent on the board size (it sets a minimum of 2 directors) of public listed companies in Kenya. The CMA guidelines on corporate governance practices (2002, p.125) however provide that:

*“The size of the board should not be too large to undermine an interactive discussion during boarding meetings or too small such that the inclusion of a wider expertise and skills to improve the effectiveness of the board is compromised.”*

Ultimately, the size of the board is however a product of the company's relationships with the environment. If the organization has requirements for co-opting important external elements of its environments, the greater this need for co-optation, the more members the organization will probably have to place on its board. Pfeffer (1972) also hypothesizes that the number of directors an organization has will be directly related to the size of the organization. Thus we expected to find that as board size increases board activity would also increase to compensate for increasing process losses.

**Inside Ownership:** Inside ownership refers to the proportion of equity held by insiders. I hypothesized that if board activity is a good proxy for active monitoring by the board of directors, then board activity should be a substitute for high levels of inside ownership in disciplining managers. More specifically, as inside ownership rises insiders have incentives to protect shareholder's interest and need less supervision by the board since board activity is from the efficient contracting view, “a costly monitoring alternative”.

**Outside Directors:** The CMA corporate governance guidelines (2002) propose that a balanced board constitutes an effective board. It therefore requires that the board of directors of every listed company should reflect a balance between independent, non-executive directors and executive directors. The independent and non-executive directors should form at least one-third of the membership of the board to ensure that no individual

or small group of individuals can dominate board decision-making processes (CMA guidelines on corporate governance (2002 p124, 125)).

Thus if higher board activity facilitates better board monitoring, outside directors are more likely to demand more board meetings to enhance their ability to monitor management. In addition, in boards with more outside directors, more time is likely to be spent in briefing board members than would be required in boards with higher inside directors. Thus, there should be a positive relationship between the representation of outside directors on the board and the level of board activity.

The CMA corporate guidelines (2002) defines independent” and “non-executive” directors as follows:- (Clauses 2.1.4.1 p.124-5)

An “independent director” means a director who:-

has not been employed by the company in an executive capacity within the last five years; is not affiliated to an adviser or consultant to the company or a member of the company’s senior management or a significant customer or supplier of the company or with a not-for-profit entity that receives significant contributions from the company, or within the last five years has not had any business relationship with the company (other than service as a director) for which the company has been required to make disclosure; has no personal service (contracts) with the company, or a member of the company’s senior management; is not employed by a public company at which an executive officer of the company serves as a director; is not a member of the immediate family of any person described above; or has not had any of the relationships described above with any affiliate of the company.

A “non-executive director” means a director who is not involved in the administrative or managerial operations of the company. (CMA corporate guidelines (2002; p125 clause 2.1.4.2).

**Unaffiliated owners of large equity blocks:** We define unaffiliated block holders as those shareholders owning more than five per cent of common stock, whether persons or institutions that are not related to firm executives and their relatives, or employee stock ownership plans. This information is in the company’s annual reports.

**Board Committees:** The CMA proposes that the board should establish relevant committees and delegate specific mandate to them. (CMA guidelines on corporate governance (2002 p.124 clause 2.1.1). It specifically recommends the establishment of audit and nominating committees. The PSIST (1991) recommends that these committees should mainly comprise independent non-executive directors due to the potential for conflict of interest.

An increase in the amount of delegation by the board, proxied by the total number of standing committees is likely to decrease the amount of work the board performs directly as a group. This may however increase the need for coordination and supervision by the board.

**Leadership Structure:** All the companies quoted in the Nairobi Stock Exchange have separated the roles of the Chairman and the CEO (Jebet, (2001)). It is expected that as in

the case of outside directors, an outside board chairman needs to be informed more frequently. Thus, if the intensity of the board activity measures the quality of the board's monitoring, boards with an outsider chairman should meet more frequently.

**Directors' Incentive Plans:** Director incentive plans have become an increasingly popular measure for inducing outside directors to improve their monitoring performance. If such plans motivate directors to become better monitors as suggested by Perry (1996), and board activity measures the quality of the board's monitoring, then all else being equal, board activity is expected to be higher where such plans are in use.

**The Number of other Directorships held by Outside Directors:** The CMA corporate governance guidelines (2002, p 124, clause 2.1.6) prohibit a person from holding more than five directorships in any public listed company at one time. They also recommend that no person should hold more than two chairmanships in any public listed company at any one time so as to ensure effective participation in the company's affairs. It is hypothesized that board meeting frequency is negatively related to the "business" of directors.

## 2.5 Empirical Studies

One important theme of this research has been the study of the link between ownership structure and firm performance. Morck et al.(1988) and McConnel and Servaes (1990) using Tobin's Q as a measure of firm performance, find a nonlinear relationship between ownership structure and firm performance in the USA, with management being aligned with shareholder interests at relatively high and low equity levels with signs of entrenchment at the intermediate levels.

Results from UK studies however are inconclusive, as some researchers (Short and Keasey, 1999) find results similar to those of Morck et al. in the US. On the other hand, Faccio and Lasfer (1999) and Weir, Laing and McKnight (2002) do not find any relationship between ownership structure and firm performance.

The second strand of research on the governance/ performance link focuses the association between board characteristics and firm performance. The board's oversight role is meant to mitigate the agency conflict between shareholders and top management (Jensen and Mecklin 1973).

To perform their monitoring and oversight roles effectively, board committees are supposed to be composed of "independent" directors, who are mainly outside or non-executive. Studies on whether independent boards lead to better performance have returned mixed results. In the US, Hermalin and Weisbach (1991) and Bhagat and Black (1999) find no significant relationship between board characteristics and firm performance, while Rosenstein and Wyatt (1990) find favorable stock market response to announcements of appointment of outside directors.

In the UK, following Cadbury report recommendation Vafeas and Theodorou (1998) find no relationship between board characteristics (ratio of non executive directors, board stock holdings, and chairman / CEO duality) and firm value. Weir, Laing and McKnight

(2002) who conducted cross sectional analysis of 311 UK firms do not find any significant relationship between performance and governance variables including board variables.

Aggarwal and Knoeber (1976) ascribe the apparent weak link between performance and governance to the endogeneity problem, which implies that the system is in equilibrium with respect to the governance choices.

Khanna and Palepu (1999), and Sarkar and Sarkar (1998) and Chhiber and Majmudar (1999) report on the relationship between profitability and value of Indian firms and the effect of corporate governance. Claessens and Djankov (1999) study corporate governance in transitional economies (Czech) and conclude that firms with concentrated ownership, foreign ownership, and ownership by non-bank, financial investment funds are more profitable and have higher labour productivity. Gibson (2003) found that CEOs of emerging market firms are likely to lose their jobs because of poor performance but that this sensitivity of job security to firm performance is dampened when the firm has a major domestic shareholder.

A final strand of research on the link between performance and governance seeks to construct corporate governance indices which are then correlated to performance/value. One such study is by Gompers et al. (2003), who use a set of governance provisions to construct a firm level index to proxy for shareholder rights. The researchers find that firms with strongest shareholder rights outperform those with the weaker rights. In related study, Gillan, Hartzell, and Starks (2003) report results that support a positive relationship between higher board monitoring and greater industry growth opportunities, and negative relationship between board index product uniqueness, implying that industries with unique products are less likely to have high board monitoring. They also find that industries with greater financial leverage have less restrictive governance structures.

Using the index approach, and set in an emerging markets context, Klapper and Love (2002) investigate the relationship between governance and firm performance and report that good governance is positively correlated with market valuations (Tobin's Q) and operating performance (ROA) especially in countries with weaker legal systems. A more recent study by Black, Jang and Kim (2005) develop a comprehensive corporate governance index for a cross section of 515 firms on the Korean Stock Exchange. Testing directly for the endogeneity of their index, they do not find evidence of endogeneity in their governance index, which is found to be significantly positively correlated with higher firm value. Padgett and Shabbir (2005), develop a non-compliance index for a panel of companies which are constituents of the FTSE 350 from 2000 to 2003. The researchers found that noncompliance index is exogenous, and that greater non-compliance with the UK Code implies lower total shareholder returns in their sample of companies.

### **3. RESEARCH METHODOLOGY**

#### **3.1 Research Design**

This was an analytical study of the relationship between the value, and the corporate governance rating, of companies listed at the NSE. The ratings of companies was calculated and the correlation tested between performance and corporate governance.

#### **3.2 Population And Sample**

The population of the study was all companies listed at the NSE, for the period 2003 to 2007 using panel data. We focused only on companies that have been listed continuously for the coverage period 2000-2007. This will make a sample of about 35 companies out of the population of listed companies numbering 55.

#### **3.3 Operational Definition of Variables**

##### **3.3.1. Corporate governance quality**

This study employed the proxy for corporate governance quality originally built by Leal and Carvalhal-da-Silva (2007). (Efforts have been made to ensure the index construction has been adapted to Kenyan situation and is in line with CMA guidelines). Leal and Carvalhal-da-Silva created an index called “ Corporate Governance Practices Index” (CGI). The Kenyan version which bears the acronym, KCGI, is computed from the responses to forty five binary and objective questions, all of them assessed using publicly available secondary data. Each positive answer added one point, so that the final score for each firm ranges from 0 to 45 (worst to best corporate governance quality). The index was constructed, taking into account four dimensions deemed important by the literature to assess corporate governance quality: disclosure; board composition and functioning; ethics and conflicts of interest; and shareholder rights. Appendix 1 shows the list of questionnaires used to construct the index (KCGI).

This study used an equally weighted version of the index because it is easier to reproduce. Also, although equally weighting all 45 questions entailed a subjective evaluation, it has been argued in the literature that this procedure is probably less questionable than imposing more complex weighting schemes.

##### **3.3.2. Firms’ performance**

The study used three measure of firm performance:

First, the firm’s performance was measured by a simplified version of Tobin’s Q approximated by Market to book value.

$$\text{Tobin's Q} = \text{Market equity} / \text{Book equity.}$$

Secondly, the firm’s performance was measured by return to total assets.

$$\text{ROA (return on assets)} = \text{Earnings before interest and taxes (EBIT)} / \text{book value of assets}$$

Thirdly, another measure of profitability used is the return to equity.

$$\text{ROE (return on book equity)} = \text{Net income} / \text{book value of equity.}$$

##### **3.3.3 Other governance related variables**

The model used other governance related variables namely board size, block holdings, director shareholdings, while controlling for leverage and firm size – variables which may affect the firm performance:

\***board size**; The negative relationship between board size and performance is one of the few empirical regularities in corporate finance. Board size was measured by the number of directors on the company's board.

\***block holdings**; Block holders include institutional shareholders who hold over 22.5 of a company's equity.

**Director ownership**: Following Padget and Shabbir (2005), the current study included directors' ownership (cumulative) above 3% as a control. variable

\***leverage**; was measured by the ratio of total liability to total assets.

\***Size**. The log of Total sales was used as a measure of size.

### 3.3.4 The model

Accordingly, the full model to be tested was the following:

$$FirmPerformance = \beta_1 CGI + \beta_2 brdsize + \beta_3 size + \beta_4 lev + \beta_5 blockhldings + \beta_6 directrhlding$$

## 3.4 Data Analysis

### 3.4.1 Index and sample analysis

Objective 1 was achieved by analyzing the descriptive statistics on the CGI for each of the five years of the study. The trends in the behavior of the index of the period were examined as were the year-on-year changes in the index for different firms for different years.

### 3.4.2 Link between corporate governance and performance

To investigate the link between compliance with the guideline and firm performance, the model in section 3.3.4 was applied. The regression results of performance on the explanatory variables was analyzed at various significance levels (0.10, 0.05, and 0.01). t-statistics were used to test the strength of the relationships, especially between the index and performance. We tested for endogeneity and multi-collinearity using correlation coefficient table.

## 4. DATA ANALYSIS AND FINDINGS

### 4.1 Sample Selection

The study aimed at documenting the financial statement disclosures of the 54 companies listed at the NSE for their financial years ending in the calendar year 2007. The library of the CMA was the chief source of the statements. The library did not have several copies of financial statements of several companies. The affected companies were approached and where possible provided the statements. In all, the researcher was able to access the statements of 35 companies which form the basis of the study. Table 1 summarizes the results of the sampled companies.

### 4.2 Analysis Corporate Governance Disclosures

While there is increasing tendency to disclose different aspects of corporate governance, the disclosure practices and the content of disclosures among the selected companies did not vary widely. It appears most listed companies have converged in their reporting practices. Two factors contributing to the convergence can be cited. First is the effect of the issuance of the CMA guideline which, though voluntary, nevertheless had a compelling influence, with companies striving to comply. Second is the fact that almost all companies on the NSE are audited by about four audit firms in the "big Five" league. This narrows the areas of discretion.



<b>Table 1: Corporate Governance Disclosure Index Questionnaire Checklist.</b>			
Financial statements were examined to determine whether or not they report on the disclosure issues listed below. 'YES' scored 1, while 'NO' scored 0.			
<b>DISCLOSURE ITEM</b>	<b>TOTAL SCORE</b>	<b>TOTAL POSSIBLE SCORE</b>	<b>% OF SCORE</b>
<b>I. Financial Disclosures:</b>			
1. Financial and Operating Results	35	35	<u>1</u>
2. Related Party Transaction	<u>33</u>	<u>35</u>	<u>.945</u>
3. Critical accounting policies	<u>35</u>	<u>35</u>	<u>1</u>
4. Corporate reporting framework	<u>6</u>	<u>35</u>	<u>.171</u>
5. Statement of directors' responsibility	<u>33</u>	<u>35</u>	<u>.945</u>
6. Risk and estimates in preparing and presenting financial statements	<u>6</u>	<u>35</u>	<u>.8</u>
7. Segment reporting	<u>28</u>	<u>35</u>	<u>.8</u>
8. Information regarding future plan	<u>19</u>	<u>35</u>	<u>.543</u>
9. Dividend	<u>35</u>	<u>35</u>	<u>1</u>
<b>TOTAL SUBINDEX - DISCLOSURES</b>	<b><u>230</u></b>	<b><u>315</u></b>	<b><u>73.06</u></b>
<b>II. Non- financial disclosures</b>			
<b>A. Company Objectives:</b>			
10. Information about company objectives	<u>10</u>	<u>35</u>	<u>.286</u>
<b>B. Ownership and Shareholders' Rights:</b>			
11. Ownership Structure	<u>34</u>	<u>35</u>	<u>1</u>
12. Shareholder Rights	<u>35</u>	<u>35</u>	<u>1</u>
13. Size of board	<u>35</u>	<u>35</u>	<u>1</u>
14. Composition of board	<u>35</u>	<u>35</u>	<u>1</u>
15. Division between chairman and CEO	<u>34</u>	<u>35</u>	<u>.971</u>
16. Chairman Statement	<u>35</u>	<u>35</u>	<u>1</u>
17. Information about Independent Director	<u>23</u>	<u>35</u>	
18. Role and functions of the board	<u>30</u>	<u>35</u>	<u>.857</u>
19. Organizational Hierarchy	<u>12</u>	<u>35</u>	<u>.343</u>
20. Changes in Board Structure	<u>16</u>	<u>35</u>	<u>.457</u>
21. Compliance with different legal rules	<u>35</u>	<u>35</u>	<u>1</u>
22. Audit committee	<u>35</u>	<u>35</u>	<u>1</u>
23. Remuneration committee	<u>32</u>	<u>35</u>	<u>.914</u>
24. Any other committee	<u>32</u>	<u>35</u>	<u>.914</u>
25. Composition of the committee	<u>29</u>	<u>35</u>	<u>.829</u>
26. Functioning of the committee	<u>31</u>	<u>35</u>	<u>.886</u>
27. Organizational code of ethics	<u>14</u>	<u>35</u>	<u>.4</u>
<b>TOTAL SUBINDEX - SHAREHOLDER RIGHTS</b>	<b><u>520</u></b>	<b><u>630</u></b>	<b><u>82.5</u></b>
<b>D. Members of the Board and key executives:</b>			
28. Biography of the board members	<u>22</u>	<u>35</u>	<u>.629</u>
29. No. of directorship held by individual members	<u>2</u>	<u>35</u>	<u>.057</u>
30. No. of board meeting	<u>24</u>	<u>35</u>	<u>.686</u>
31. Attendance in board meeting	<u>8</u>	<u>35</u>	<u>.229</u>

32. Director stock ownership	<u>11</u>	<u>35</u>	<u>.314</u>
33. Director remuneration	<u>28</u>	<u>35</u>	<u>.229</u>
<b>TOTAL SUBINDEX-BRD STRUCTURE</b>	<b><u>95</u></b>	<b><u>210</u></b>	<b><u>45.238</u></b>
<i>E. Material issues regarding employees, environmental and social stewardship</i>			
34. Employee relation/Industrial relation	<u>24</u>	<u>35</u>	<u>.686</u>
35. Environmental and social responsibility	<u>25</u>	<u>35</u>	<u>.714</u>
<i>F. Material foreseeable risk factors:</i>			
36. Risk assessment and management	<u>28</u>	<u>35</u>	<u>.800</u>
37. Internal control system	<u>17</u>	<u>35</u>	<u>.486</u>
38. Auditor appointment and rotation	<u>30</u>	<u>35</u>	<u>.943</u>
39. Auditor fees	<u>33</u>		
<b>III. Annual General Meeting:</b>			
40. Notice of the AGM	<u>34</u>	<u>35</u>	<u>.971</u>
41. Agenda of the AGM	<u>34</u>	<u>35</u>	<u>.971</u>
<b>IV. Timing and means of disclosure:</b>			
42. Separate Corporate Governance statement/ separate section for corporate governance	<u>34</u>	<u>35</u>	<u>.971</u>
43. Annual report through internet	<u>34</u>	<u>35</u>	<u>.971</u>
44. Any other event	<u>31</u>	<u>35</u>	<u>.886</u>
45. Compliance with CMA notification	<u>20</u>	<u>35</u>	<u>.57</u>

As seen in Table 2 and Table 3, the range in the disclosure item scores among the selected companies is narrow. With a maximum of 45 disclosure items and the average score of 32.74, or 72.75%, one company received the highest score of 41 or 89%. At the low end, also one company received a score of 26, or 55.55%.

To assess whether an equal weighting scheme is appropriate, Table 2 shows the correlation matrix for all sub-indices (i.e., the ratings of the five governance categories in our survey). All correlations are positive, but in general not very high. This indicates that our weighting scheme avoids double-counting by assigning undue weights to some governance practices (while neglecting others), which would lead to biases in our aggregate rating. Only the correlation between the categories ‘board structure and functioning’ and ‘shareholder rights’ are above 0.5. This, however, should not impose a problem, because these two governance categories are hardly regarded as substitutes.

### 4.3 Constructing A Kenyan Corporate Governance Index

We use a broad, multifactor corporate governance index (CGI), which is based on scores to objective governance survey questions in Table 1. These questions cover aspects of corporate governance recommended by Capital Markets Authority (2002), Guidelines on Corporate Governance in Public Listed Companies in Kenya.

In total, we collect 45 governance proxies divided into four categories: (1) Disclosures (financial), (2) Board structure and functioning, (3) Ethics, and (4) Shareholder rights.

For each firm the aggregate rating is an unweighted sum of the points across all proxies, ranging from 0 (minimum) to 45 (maximum). Tables 1 shows the resulting descriptive statistics of the corporate governance index. The rating over the 35 firms in our sample is slightly skewed to the left. More than 40% of the firms have a rating between 34 and 37. It should also be noted that an equal weighting scheme for the different proxies makes no attempt to accurately reflect the relative importance of individual governance practices, but it has the advantage of being transparent and allows easy interpretations.

**Table 2** Frequency Distribution of Total Score by Individual Company. The total scores are determined as set out in Table 3

Total Score	N	Cum. N	%	Cum. %
21-25	1	1	2.94	2.94
26-30	8	9	23.53	26.47
31-35	19	28	55.88	82.35
36-40	7	35	17.65	100

*Source: Compiled and Computed from the Annual Report of the Concerned Company*

**Table 3: Descriptive statistics of the KCGD Index**

Mean	33.71429
Median	34
Mode	35
Standard deviation	3.214
Kurtosis	0.145523
Skewness	-0.14305
Range	15
Minimum	26
Maximum	41
Count	34

#### 4.4 Results for Control Variables, Subindices, and Board Composition

We return in this part to *OLS*, and describe results for the control variables we use in our base *OLS* regression (Section A). We then consider the predictive power of each subindex (Section B), individual governance elements (Section C), and board composition in particular (Section D). Two important results emerge. First, the power of *KCGI* is not sensitive to how we construct this index, and comes from the cumulative effect of all five sub-indices. Second, Kenyan firms, with 50% outside directors have significantly higher share prices than firms with fewer outside directors. This effect appears to be causal. This is strong evidence that greater board independence predicts higher share prices in emerging markets.

#### 4.5 Results For Control Variables

Extensive control variables were used to limit omitted variable bias, as well as the potential for the optimal differences flavor of endogeneity. The rationale, and *OLS* regression results, shown in Table 3 for each control variable are described below.

**Firm size.** Consistent with prior research (e.g., Lang and Stulz, 1994), the coefficient on  $\ln(\text{SALES})$  is negative and highly significant. Our results are similar if we substitute  $\ln(\text{ASSETS})$  for  $\ln(\text{SALESs})$ , or use a 6 powers functional form of  $\ln(\text{assets})$  or  $\ln(\text{sales})$ .

**Age ( $\ln(\text{years listed})$ ).** Older firms could differ from younger firms both in Tobin's  $q$  and governance practices. We therefore include  $\ln(\text{years listed})$  as a control variable. We expected a negative coefficient because younger firms are likely to be faster-growing and perhaps more intangible asset-intensive. This variable is negative and significant.

**Firm leverage.** Leverage can affect both Tobin's  $q$  and a firm's governance practices. Governance may also affect a firm's access to credit (Bhojraj and Sengupta, 2003). We control for debt/market value of equity (when we use market/book as a dependent variable, we use debt/book value of assets as a control variable). This control is positive and significant.

**Profitability.** Profitability is likely to be related to Tobin's  $q$ . We therefore control for operating margin, defined as EBIT/sales. This variable is positive but insignificant.

**Block holdings.** Share ownership is an important element of corporate governance, but the relationship between ownership and firm value is unclear and possibly nonlinear. We control for ownership by the largest shareholder (whether an individual or a firm), and ownership<sup>2</sup>. Neither variable is significant

**Board size.** Our results are similar if we include board size as a control variable. We consider board size variable as number of directors;. Board size is insignificant.

**Kenya corporate governance index (KCGI).** Our results are similar if we include a subjective corporate governance index, which we construct based on 45 questions in our guide on various corporate governance issues. The subjective index could predict firm value and performance because management attitudes influence investor beliefs about management quality, or because it proxies for governance elements that were omitted from *KCGI*. The coefficient on the subjective index is small and insignificant.

**Table 4: Regression estimates of the full model for all dependent variables.**

This table shows the results of OLS heteroscedasticity-consistent estimations of the determinants of firm-level market valuation. The dependent variables are Tobin's Q, Return on Assets, and the Return on Equity. The regressor variables are defined as follows: ln(SALES) denotes the logarithm of sales ((for the year 2007), BORD SIZE is the number of board members for 2007 ln(AGE) is the number of years listed on the German stock exchange, and LEVERAGE is computed as the ratio of total liabilities to total assets (end 2007) BLOCK HOLDING is the proportion of share capital of over 22.5% held by an individual or institution and DIRECTOR HOLDING is proportion of capital held by directors

<b>Explanatory</b>	<b>Dependent-Tobin's Q</b>	<b>Dependent-ROA</b>	<b>Dependent-ROE</b>
CGDI	-2.09** (-2.01)	-.37 (-.82)	.73 (.40)
Board size	-.37 (-.54)	-1.22*** (-4.13)	-1.95 (-1.5)
Size- log(SALES)	-.0033 (-1.58)	.0019 (1.69)	.0023 (.62)
Leverage	-4.51 (-.44)	-11.21*** (-2.62)	-65.28**** (-3.73)
Block holdings	-.06 (-.60)	-.02 (.70)	-.03 (-.19)
Director holdings	-.11 (-.73)	-.04 (-.42)	0.21 (.69)
R-squared	.26	.07	.042
No. of observations	35	35	35

\*, \*\*, \*\*\* denote significance at the 0.10, 0.05, and 0.01 level. t-statistics are in parenthesis

**Table 5: Descriptive statistics for all variables used in the analysis**

<b>Variable</b>	<b>Minimum</b>	<b>Maximum</b>	<b>Mean</b>	<b>Median</b>	<b>S. Deviation</b>
<b>Dependent</b>					
Tobin's	0.49	0.49	3.225313	2.89	2.327164
ROA %	-0.23	0.3	0.069618	0.06	0.084694
ROE %	-6.35	0.54	5.88E-05	.16	1.127262
<b>Explanatory</b>					
CGDI	26	41	33.71429	34	3.213679
Board size	5	17	10.14286	10	2.745508
Log( sales)	20.50621	27.368	22.45333	22.2154	1.298008
Debt to assets ratio	0.01	.89	0.550588	.515	0.232626
Block holdings	0	.82	0.425588	.45	0.239547

Table 6: Descriptive statistics of the formulae and sub-indices

$$ROA, ROE = \beta_0 + \beta_1 KCGI + \beta_2 BRDSZ + \beta_3 LNSALE + \beta_4 LEV + \beta_5 BLCK + \beta_6 DRCT :$$

	minimum	maximum	mean	std. dev	kurtosis	skew
ROA	-0.23	0.3	0.066273	0.083696	5.455427	-0.49726
ROE	-6.35	0.54	5.88E-05	1.127262	33.3152	-5.74414
KCGI	26	41	33.71429	3.213679	0.145523	-0.14305
BRDSIZE	5	17	10.14286	2.745508	0.084614	0.104098
LNSA-SIZE	20.50621	27.36778	22.45333	1.298008	4.978955	1.598582
LEV	0.01	0.89	0.550588	0.232626	-0.59611	-0.0897
BLCKHLDG	0	0.82	0.425588	0.239547	-0.65979	-0.4298
DRCTHLDG	0	0.82	0.132824	0.234741	1.785192	1.69139
<b>SUBINDICES</b>						
DSCSR	4	8	6.571429	0.884032	0.990635	-0.63581
SHRHRGHT	10	17	14.57143	1.719879	0.182218	-0.75382
BRDSTR	0	6	2.714286	1.426048	-0.58567	0.15147
ETHICS	0	12	9.428571	2.186667	9.378435	-2.30558
Directors holdings	0	.82	0.132824	0	0.234741	
Firm age	1	57	23.25714286	21	16.19067	

### Results for Sub indices and Reduced Indices

Table 4 contains our *OLS* results for sub-indices. In row (1), we regress Tobin's *q* on each of our five sub-indices, included one at a time in separate regressions, in each case replacing *KCGI* in our base *OLS* regression: Each sub-index is significant at the 1% level or better.

In row (2), we control for the other sub-indices by adding, as a control variable for each sub-index, a Reduced Index (0~80) that equals (*KCGI* - indicated sub-index). We show results for sub-indices in row (2A) and for each Reduced Index in row (2B). All sub-indices have positive coefficients, but the coefficients and *t*-statistics decline, as expected. Board Structure and Disclosure sub-indices remain significant. Shareholder Rights Sub-index is marginally significant. In row (3), we include all five sub-indices in a single regression, with similar results.

**Table 7: OLS Results for Sub-indices**

Ordinary least squares regressions of Tobin's q on KCGI and each sub-index. Control variables and sample (n = 494) are the same as in our base OLS regression. In row (1), we replace KCGI with the indicated sub-index, without a separate control for the rest of the corporate governance index. In row (2), we add a control variable for a "Reduced Index" which equals the sum of the other four sub-indices. In row (3), we include all five sub-indices as separate independent variables. \*, \*\*, and \*\*\* respectively indicate significance levels at 10%, 5%, and 1% levels. T-values, based on White's heteroskedasticity-consistent standard errors, are reported in parentheses. Adjusted R2 is shown for each regression. Significant results (at 5% level or better) are shown in boldface

<b>KCGI or Sub-index</b>	<i>KCGI</i>	<i>Fin. disclosure</i>	<i>Share holder right</i>	<i>Board structure</i>	<i>Ethics</i>
<i>dependent variable: Tobin's q</i>	0.0064** (2.77) .2832	0.0066*** (3.73) .2973	0.0089*** (3.13) .2906	0.0116*** (3.23) .2705	0.0084*** (6.12) .3334
Coefficient on sub index, with control for Reduced Index		0.0040* (1.73) .3343	<b>0.0070***</b> <b>(3.08)</b> <b>.3329</b>	0.0051 (1.31) .3330	<b>0.0060**</b> <b>(3.28)</b> <b>.3345</b>
2B Coefficient for Reduced Index (sum of remaining sub indices) (from same regression as column 2A)		<b>. 0.0072***</b> <b>(5.62)</b> 0.3345	<b>0.0062***</b> <b>(5.14)</b> 0.3329	<b>0.0067***</b> <b>(5.06)</b> 0.3330	<b>0.0065***</b> <b>(5.51)</b> <b>0.0067***</b> 0.3328
3 Coefficients from single regression with all sub indices		0.0043* (1.73) 0.3320	<b>0.0068***</b> <b>(2.92)</b> 0.3320	0.0052 (1.33) 0.3320	<b>0.0062**</b> <b>(2.48)</b> 0.3320

**Table 8: Descriptive statistics of sub-indices**

	Minimum	maximum	mean	Std. deviation	kurtosis	skew
Financial disclosure	4	8	6.57	0.884	0.99	-0.636
Shareholder rights	10	17	14.57	1.72	0.182	-0.754
Board structure	0	6	2.71	1.43	-0.586	0.151
Ethics	0	12	9.43	2.19	9.38	-2.306

Since each sub index is significant in row (1), almost any weighting will produce an overall index that is significant in explaining Tobin's  $q$ . Moreover, the coefficients on sub indices are similar in magnitude, ranging in row (1) from .0064 to .0133 and in row (3) from .0040 to .0106. Thus, subindex weights are unlikely to greatly affect the coefficient or significance of *KCGI*.

We confirm the intuition that our results for *KCGI* are not sensitive to subindex weights in two ways. First in row (2B), each Reduced Index is statistically strong, and coefficients vary only from 0.0057 to 0.0072. The significance of each Reduced Index is lower than for *KCGI*. This is consistent with the predictive power of *KCGI* reflecting the combined effect of all subindices, including the less powerful Shareholder Rights and Board Procedure subindices.

This optimal index is:

$$KCG\ I_{optimal} = 0.1303 * \text{Shareholder Rights Index} + 0.2061 * \text{Board Structure Subindex} + 0.1576 * \text{Ethics sub-index} + 0.1879 * \text{Disclosure Subindex}.$$

This optimal index would take an *OLS* coefficient of .0064 ( $t = 6.12$ ), only modestly higher than the coefficient of .0066 ( $t = 6.30$ ) for actual *KCGI*.

<b>Table 9: Correlation matrix for corporate governance sub-indices</b>				
This table shows the correlations among the five corporate governance sub-indices. The aggregate corporate governance rating (CGR) consists of governance proxies in four categories: (i) financial disclosure, (ii) shareholder rights (iii) board structure and functioning and (iv) ethics. Each sub-index is constructed using an equal weighting scheme for the respective survey questions.				
	Financial disclosure	Shareholder rights	Board structure	Ethics
Financial disclosure	1.000			
Shareholder rights	0.205823	1.000		
Board structure	0.063325	0.584178	1.000	
Ethics	0.052166	0.347458	0.285655	1.000

## 5. CONCLUSIONS, RECOMMENDATIONS AND LIMITATIONS

### 5.1 Conclusions

In this paper, we report evidence that corporate governance is an important factor in explaining the market value of NSE listed companies, and that this effect is likely causal. We construct a corporate governance index (*CGI*, 0~100) for 35 of the 55 companies listed on the Nairobi Stock Exchange. We employ extensive control variables. We find an economically significant correlation between *CGI* and firm market value.



The regression discontinuity approach (borrowed from labor economics) is potentially generalizable to other corporate governance research. It can apply whenever corporate governance rules change based on a numerical criterion such as firm size. We also find evidence that Kenyan firms with 50% outside directors are more highly valued. Firms with 50% outside directors have 0.13 higher predicted Tobin's  $q$  (roughly 40% higher share price), with similar coefficients for firms for whom 50% outside directors are mandatory and firms that voluntarily adopt this practice. This suggests that outside directors can be valuable in an emerging market country, even if the outside director requirement is imposed by law rather than voluntarily chosen.

Better corporate governance does not appear to predict higher firm profitability. It does appear to predict lower cost of external capital, perhaps because investors expect insiders to engage in less self-dealing. It is an open question to what extent the higher share prices of better governed firms reflect an increase in total firm value, versus a decline in private benefits of control enjoyed by insiders.

## **5.2 Recommendations for the Future**

From the findings of the study, it is evident that corporate reporting by listed companies in the country is of a satisfactory level. But we need to take cognizance of several challenges.

1. Disclosure alone in the annual reports shall not be enough. Practice of good corporate governance must also be emphasized. Practice together with disclosure can facilitate and stimulate the performance of companies, limit the insiders' abuse of power over corporate resources and provide a means to monitor managers' opportunistic behavior.
2. Within the current type of analysis, scope may be widened by covering the corporate governance disclosure practice by Kenyan public limited companies over a number of years to find out the extent of importance the organizations are emphasizing on this issue.
3. The CMA guideline has had an impact on the reporting practices of quoted companies; so has Central Bank requirements on the financial statement of financial institutions. The majority of business organizations, however, fall outside the purview of the CMA and the Central Bank. There is need to assess the gaps and loopholes in the governance and related reporting for such private companies. Scholarly effort should be directed in this sector.
4. Further research is necessary using time series techniques and panel data to evaluate the improvements and trends over time. This can help ascertain the drivers , (or impediments) to advancement in proper governance practices and reporting.
5. Further analysis may also include managerial perceptions studies and stakeholders' perceptions studies.
6. Steps should be taken for mandatory compliance of the CMA notification and for reducing the gap between disclosure practices especially for companies not quoted at NSE.

### 5.3 Limitations of the Study

The findings of the study may be limited in the generalizability because of several data and methodological weaknesses:

1. First, the whole population of the 54 listed companies could not be studied because of inaccessibility of their financial statements. A clearer picture of the companies' practices would be gleaned only if the full population were used.
2. Moreover, in this project all the disclosure items are given same weight. Although this helps to reduce subjectivity, the market may place higher emphasis on certain elements of governance.
3. Also, some aspect of governance may be considered to be a basic component or prerequisite to implementing others and thus should be given more weight.

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APPENDIX 1													
Corporate Governance Disclosure Index Questionnaire Checklist.													
Financial statements will be examined to determine whether or not they report on the disclosure issues listed below. 'YES' will score 1, while													
DISCLOSURE ITEM	uni	kaku	rea	c&g	cmc	kq	nng	scan	tps	uchu	bbk	centu	cf
<b>I. Financial Disclosures:</b>													
1. Financial and Operating Results	1	1	1	1	1	1	1	1	1	1	1	1	1
2. Related Party Transaction	1	1	0	1	0	1	1	1	1	1	1	1	1
3. Critical accounting policies	1	1	1	1	1	1	1	1	1	1	1	1	1
4. Corporate reporting framework	1	0	0	0	0	0	0	0	1	0	0	0	0
5. Statement of directors' responsibility	1	1	1	1	1	1	1	1	0	1	1	1	1
6. Risk and estimates in preparing and presenting financial statements	0	0	1	0	0	0	0	1	0	0	1	0	0
7. Segment reporting	0	1	1	1	1	1	1	1	1	1	1	1	1
8. Information regarding future plan	0	0	0	1	1	1	1	0	0	0	1	0	0
9. Dividend	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>TOTAL SUBINDEX - DISCLOSURES</b>	<b>6</b>	<b>6</b>	<b>6</b>	<b>7</b>	<b>6</b>	<b>7</b>	<b>7</b>	<b>6</b>	<b>7</b>	<b>6</b>	<b>8</b>	<b>6</b>	<b>6</b>
<b>II. Non-financial disclosures</b>													
<b>A. Company Objectives:</b>													
10. Information about company objectives	0	1	0	1	0	0	0	0	0	0	1	0	0
<b>B. Ownership and Shareholders' Rights :</b>													
11. Ownership Structure	1	1	1	1	1	1	1	1	1	1	1	1	1
12. Shareholder Rights	1	1	1	1	1	1	1	1	1	1	1	1	1
13. Size of board	1	1	1	1	1	1	1	1	1	1	1	1	1
14. Composition of board	1	1	1	1	1	1	1	1	1	1	1	1	1
15. Division between chairman and CEO	1	1	1	1	1	1	1	1	1	1	1	1	1
16. Chairman Statement	1	1	1	1	1	1	1	1	1	1	1	1	1
17. Information about Independent Director	1	0	1	0	0	1	1	1	1	0	1	1	1
18. Role and functions of the board	1	1	1	1	1	1	0	0	1	1	0	1	1
19. Organizational Hierarchy	0	0	0	0	1	0	0	0	0	0	0	0	1
20. Changes in Board Structure	1		0	0	0	1	1	0	0	1	0	1	1
21. Compliance with different legal rules	1	1	1	1	1	1	1	1	1	1	1	1	1
22. Audit committee	1	1	1	1	1	1	1	1	1	1	1	1	1
23. Remuneration committee	1	1	1	1	1	1	1	1	1	1	1	1	1
24. Any other committee	1	1	1	0	1	1	1	1	1	1	1	1	1
25. Composition of the committee	1	0	1	0	1	1	1	1	1	1	1	1	1
26. Functioning of the committee	1	1	1	1	1	1	0	1	1	1	1	1	1
27. Organizational code of ethics	1	0	0	0	0	1	0	0	0	0	0	0	0
<b>TOTAL SUBINDEX - SHAREHOLDER RIGHTS</b>	<b>16</b>	<b>13</b>	<b>14</b>	<b>12</b>	<b>14</b>	<b>16</b>	<b>13</b>	<b>13</b>	<b>14</b>	<b>15</b>	<b>13</b>	<b>16</b>	<b>16</b>
<b>D. Members of the Board and key executives:</b>													
28. Biography of the board members	1	0	1	0	0	1	1	0	1	0	1	1	1
29. No. of directorship held by individual members	0	0	0	0	0	0	0	0	0	0	0	0	0
30. No. of board meeting	1	0	1	1	1	1	0	1	1	1	0	1	1
31. Attendance in board meeting	0	0	0	0	0	0	0	0	0	0	0	0	1
32. Director stock ownership	0	0	0	1	0	1	0	0	1	0	0	0	1
33. Director remuneration	1	1	1	1	1	1	0	1	1	1	1	0	1
<b>TOTAL SUBINDEX-BRD STRUCTURE</b>	<b>3</b>	<b>1</b>	<b>3</b>	<b>3</b>	<b>2</b>	<b>4</b>	<b>1</b>	<b>2</b>	<b>4</b>	<b>2</b>	<b>1</b>	<b>5</b>	<b>5</b>
<b>E. Material issues regarding employees, environmental and social stewardship</b>													
34. Employee relation/Industrial relation	1	1	1	1	0	1	0	0	1	0	1	0	0
35. Environmental and social responsibility	1	1	1	1	0	1	1	1	1	1	0	1	1
<b>F. Material foreseeable risk factors :</b>													
36. Risk assessment and management	1	0	0	1	1	1	1	1	1	1	1	1	1
37. Internal control system	0	0	0	1	1	1	0	1	1	1	1	0	0
<b>G. Independence of Auditors:</b>													
38. Auditor appointment and rotation	1	1	1	1	0	1	0	1	1	1	1	1	1
39. Auditor fees	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>III. Annual General Meeting:</b>													
40. Notice of the AGM	1	1	1	1	1	1	1	1	1	1	1	1	1
41. Agenda of the AGM	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>IV. Timing and means of disclosure:</b>													
42. Separate Corporate Governance statement/ separate section for corporate governance	1	1	1	1	1	1	1	1	1	1	1	1	1
43. Annual report through internet	0	0	1	0	1	1	1	1	0	0	1	0	0
44. Any other event	1	0	1	0	1	0	1	1	1	1	1	1	1
<b>V. Best practices for compliance with corporate governance</b>													
45. Compliance with CMA GUIDELINES	1	1	1	0		0	1	0	1	1	1	1	1
<b>TOTAL SUBINDEX - ETHICS</b>	<b>10</b>	<b>8</b>	<b>10</b>	<b>9</b>	<b>8</b>	<b>11</b>	<b>9</b>	<b>11</b>	<b>11</b>	<b>9</b>	<b>11</b>	<b>9</b>	<b>9</b>
<b>GRAND TOTAL</b>	<b>35</b>	<b>28</b>	<b>33</b>	<b>31</b>	<b>30</b>	<b>38</b>	<b>30</b>	<b>32</b>	<b>36</b>	<b>32</b>	<b>33</b>	<b>36</b>	<b>36</b>

<b>APPENDIX 1</b>																
<b>Corporate Governance Disclosure Index Questionnaire Checklist.</b>																
<b>Financial statements will be examined to determine whether or not they report on the disclosure issues listed below. 'YES' will score 1</b>																
DISCLOSURE ITEM	diamond	equity	hfck	jublee	kcb	k-re	nbk	nic	scb	arm	bambu	bat	ea cables	ea brewer	ea port	
<b>I. Financial Disclosures:</b>																
1. Financial and Operating Results	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
2. Related Party Transaction	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
3. Critical accounting policies	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
4. Corporate reporting framework	0	0	0	0	0	0	0	0	1	0	0	1	0	0	1	0
5. Statement of directors' responsibility	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
6. Risk and estimates in preparing and presenting financial statements	0	0	0	0	1	0	1	0	1	0	0	0	0	0	0	0
7. Segment reporting	0	1	1	1	1	1	1	1	1	0	1	0	1	1	1	0
8. Information regarding future plan	0	1	1	0	0	1	0	1	0	1	1	1	1	0	1	0
9. Dividend	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>TOTAL SUBINDEX - DISCLOSURES</b>	<b>5</b>	<b>7</b>	<b>7</b>	<b>6</b>	<b>7</b>	<b>7</b>	<b>7</b>	<b>8</b>	<b>6</b>	<b>7</b>	<b>7</b>	<b>7</b>	<b>6</b>	<b>8</b>	<b>4</b>	
<b>II. Non-financial disclosures</b>																
<b>A. Company Objectives:</b>																
10. Information about company objectives	0	0	0	0	0	0	0	0	1	0	0	1	0	0	1	0
<b>B. Ownership and Shareholders' Rights :</b>																
11. Ownership Structure	1	1	1	1	1	1	1	1	1	1	1	0	1	1	1	1
12. Shareholder Rights	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
13. Size of board	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
14. Composition of board	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
15. Division between chairman and CEO	1	1	1	0	1	1	1	1	1	1	1	1	1	1	1	1
16. Chairman Statement	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
17. Information about Independent Director	1	1	1	0	1	1	0	1	1	0	1	1	1	1	1	0
18. Role and functions of the board	1	1	1	1	1	0	1	1	1	1	0	1	1	1	1	1
19. Organizational Hierarchy	1	1	1	0	0	1	0	0	0	0	0	1	1	1	0	1
20. Changes in Board Structure	0	1	0	0	1	0	0	0	1	0	1	0	0	1	0	
21. Compliance with different legal rules	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
22. Audit committee	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
23. Remuneration committee	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
24. Any other committee	1	1	1	1	1	1	1	1	1	1	0	1	1	1	1	1
25. Composition of the committee	0	1	1	1	1	1	1	1	1	1	1	0	1	1	1	1
26. Functioning of the committee	1	1	1	1	1	1	1	1	1	0	1	1	1	1	1	1
27. Organizational code of ethics	1	1	0	1	1	1	0	1	1	0	1	0	0	0	0	1
<b>TOTAL SUBINDEX - SHAREHOLDER RGHTS</b>	<b>15</b>	<b>17</b>	<b>15</b>	<b>13</b>	<b>16</b>	<b>15</b>	<b>13</b>	<b>16</b>	<b>16</b>	<b>10</b>	<b>17</b>	<b>14</b>	<b>15</b>	<b>16</b>	<b>15</b>	
<b>D. Members of the Board and key executives:</b>																
28. Biography of the board members	1	1	1	0	1	0	0	1	1	0	1	1	1	1	1	0
29. No. of directorship held by individual members	0	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0
30. No. of board meeting	1	1	1	0	1	1	1	1	1	1	0	1	0	1	1	0
31. Attendance in board meeting	1	0	1	0	1	0	1	1	1	1	0	0	0	0	0	0
32. Director stock ownership	0	0	0	1	1	0	0	0	0	0	0	0	1	1	1	0
33. Director remuneration	1	0	1	1	1	1	1	1	1	1	1	1	0	1	0	1
<b>TOTAL SUBINDEX-BRD STRUCTURE</b>	<b>4</b>	<b>2</b>	<b>4</b>	<b>2</b>	<b>6</b>	<b>2</b>	<b>3</b>	<b>5</b>	<b>4</b>	<b>1</b>	<b>3</b>	<b>1</b>	<b>4</b>	<b>3</b>	<b>1</b>	
<b>E. Material issues regarding employees, environmental and social stewardship</b>																
34. Employee relation/Industrial relation	1	0	1	0	1	1	0	1	1	1	1	1	1	1	1	1
35. Environmental and social responsibility	1	0	0	0	1	1	0	1	1	1	1	1	1	0	1	1
<b>F. Material foreseeable risk factors :</b>																
36. Risk assessment and management	1	1	1	1	1	1	1	1	1	1	0	1	1	1	0	1
37. Internal control system	1	1	1	1	0	0	0	1	1	0	0	1	1	1	0	1
<b>G. Independence of Auditors:</b>																
38. Auditor appointment and rotation	1	1	1	1	0	1	1	1	1	1	1	1	1	1	1	1
39. Auditor fees	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>III. Annual General Meeting:</b>																
40. Notice of the AGM	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
41. Agenda of the AGM	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>IV. Timing and means of disclosure:</b>																
42. Separate Corporate Governance statement/ reports	1	1	1	1	1	1	0	1	1	0	1	1	1	1	1	1
43. Annual report through internet	1	1	0	1	1	1	1	1	1	0	1	1	0	0	1	1
44. Any other event	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1	1
<b>V. Best practices for compliance with corporate governance</b>																
45. Compliance with CMA GUIDELINES	0	1	1	1	1	0	0	1	0	0	1	1	1	1	0	1
<b>TOTAL SUBINDEX - ETHICS</b>	<b>11</b>	<b>9</b>	<b>10</b>	<b>10</b>	<b>9</b>	<b>9</b>	<b>7</b>	<b>12</b>	<b>11</b>	<b>8</b>	<b>10</b>	<b>12</b>	<b>10</b>	<b>8</b>	<b>12</b>	
<b>GRAND TOTAL</b>	<b>35</b>	<b>35</b>	<b>36</b>	<b>31</b>	<b>38</b>	<b>33</b>	<b>30</b>	<b>41</b>	<b>37</b>	<b>26</b>	<b>37</b>	<b>34</b>	<b>35</b>	<b>35</b>	<b>32</b>	

<b>Corporate Governance Disclosure Index Questionnaire Checklist.</b>												
<b>Financial statements will be examined to determine whether or not they report on the disclosure issues</b>												
DISCLOSURE ITEM	ea port	eveready	kpl&c	kengen	mumias	sameer	unga	Express	TTL	TTL	%	
									SCO	PSSBL	SCORE	
<b>I. Financial Disclosures:</b>												
1. Financial and Operating Results	1	1	1	1	1	1	1	1	1	35	35	1
2. Related Party Transaction	1	1	1	1	1	1	1	1	1	33	35	0.942857
3. Critical accounting policies	1	1	1	1	1	1	1	1	1	35	35	1
4. Corporate reporting framework	0	0	0	0	0	0	0	0	0	6	35	0.171429
5. Statement of directors' responsibility	0	1	1	1	1	1	1	1	1	33	35	0.942857
6. Risk and estimates in preparing and presenting financial statements	0	0	0	0	0	0	0	0	0	6	35	0.171429
7. Segment reporting	0	1	1	0	0	0	1	1	1	28	35	0.8
8. Information regarding future plan	0	1	0	0	1	1	1	1	1	19	35	0.542857
9. Dividend	1	1	1	1	1	1	1	1	1	35	35	1
<b>TOTAL SUBINDEX - DISCLOSURES</b>	<b>4</b>	<b>7</b>	<b>6</b>	<b>5</b>	<b>6</b>	<b>7</b>	<b>7</b>	<b>7</b>	<b>7</b>	<b>230</b>	<b>315</b>	<b>73.01587</b>
<b>II. Non-financial disclosures</b>												
<b>A. Company Objectives:</b>												
10. Information about company objectives	0	1	0	1	1	0	1	0	0	10	35	0.285714
										10		
<b>B. Ownership and Shareholders' Rights :</b>												
11. Ownership Structure	1	1	1	1	1	1	1	1	1	34	35	0.971429
12. Shareholder Rights	1	1	1	1	1	1	1	1	1	35	35	1
13. Size of board	1	1	1	1	1	1	1	1	1	35	35	1
14. Composition of board	1	1	1	1	1	1	1	1	1	35	35	1
15. Division between chairman and CEO	1	1	1	1	1	1	1	1	1	34	35	0.971429
16. Chairman Statement	1	1	1	1	1	1	1	1	1	35	35	1
17. Information about Independent Director	0	1	0	0	1	0	1	0	1	23	35	0.657143
18. Role and functions of the board	1	1	1	1	1	1	1	1	1	30	35	0.857143
19. Organizational Hierarchy	1	0	0	0	0	1	0	0	0	12	35	0.342857
20. Changes in Board Structure	0	1	1	1	1	0	1	1	1	16	35	0.457143
21. Compliance with different legal rules	1	1	1	1	1	1	1	1	1	35	35	1
22. Audit committee	1	1	1	1	1	1	1	1	1	35	35	1
23. Remuneration committee	1	1	1	1	1	1	1	1	1	35	35	1
24. Any other committee	1	1	1	1	1	1	1	0	0	32	35	0.914286
25. Composition of the committee	1	1	1	1	1	1	1	0	0	29	35	0.828571
26. Functioning of the committee	1	1	1	0	1	1	1	1	1	31	35	0.885714
27. Organizational code of ethics	1	0	0	1	0	0	1	0	0	14	35	0.4
<b>TOTAL SUBINDEX - SHAREHOLDER RIGHTS</b>	<b>15</b>	<b>16</b>	<b>14</b>	<b>15</b>	<b>16</b>	<b>14</b>	<b>17</b>	<b>12</b>	<b>12</b>	<b>520</b>	<b>630</b>	<b>82.53968</b>
<b>D. Members of the Board and key executives:</b>												
28. Biography of the board members	0	1	1	1	1	0	1	0	0	22	35	0.628571
29. No. of directorship held by individual members	0	0	0	0	0	0	0	0	0	2	35	0.057143
30. No. of board meeting	0	0	0	1	1	1	1	0	0	24	35	0.685714
31. Attendance in board meeting	0	0	0	0	0	0	0	0	0	8	35	0.228571
32. Director stock ownership	0	0	1	0	1	0	1	0	0	11	35	0.314286
33. Director remuneration	1	0	1	1	1	1	1	1	1	28	35	0.8
<b>TOTAL SUBINDEX-BRD STRUCTURE</b>	<b>1</b>	<b>1</b>	<b>3</b>	<b>3</b>	<b>4</b>	<b>2</b>	<b>4</b>	<b>1</b>	<b>1</b>	<b>95</b>	<b>210</b>	<b>45.2381</b>
<b>E. Material issues regarding employees, environmental and social stewardship</b>												
34. Employee relation/Industrial relation	1	1	1	0	1	1	0	0	0	24	35	0.685714
35. Environmental and social responsibility	1	1	1	1	1	1	0	0	0	25	35	0.714286
<b>F. Material foreseeable risk factors :</b>												
36. Risk assessment and management	1	0	1	1	0	1	1	1	1	28	35	0.8
37. Internal control system	1	0	1	0	0	0	0	0	1	17	35	0.485714
<b>G. Independence of Auditors:</b>												
38. Auditor appointment and rotation	1	1	1	1	1	1	1	1	1	30	35	0.857143
39. Auditor fees	1	1	1	1	1	1	1	1	1	33	35	0.942857
<b>III. Annual General Meeting:</b>												
40. Notice of the AGM	1	1	1	1	1	1	1	1	1	34	35	0.971429
41. Agenda of the AGM	1	1	1	1	1	1	1	1	1	34	35	0.971429
<b>IV. Timing and means of disclosure:</b>												
42. Separate Corporate Governance statement/ separate report	1	0	1	1	1	1	1	1	1	31	35	0.885714
43. Annual report through internet	1	1	1	0	0	1	0	0	0	20	35	0.571429
44. Any other event	1	1	1	1	1	1	1	1	1	30	35	0.857143
<b>V. Best practices for compliance with corporate governance</b>												
45. Compliance with CMA GUIDELINES	1	1	1	1	0	1	0	1	1	23	35	0.657143
<b>TOTAL SUBINDEX - ETHICS</b>	<b>12</b>	<b>9</b>	<b>12</b>	<b>9</b>	<b>8</b>	<b>11</b>	<b>7</b>	<b>9</b>	<b>9</b>	<b>329</b>	<b>420</b>	<b>78.33333</b>
<b>GRAND TOTAL</b>	<b>32</b>	<b>33</b>	<b>35</b>	<b>32</b>	<b>34</b>	<b>34</b>	<b>35</b>	<b>29</b>	<b>1174</b>	<b>1575</b>	<b>74.53968</b>	

