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Effect of Executive Compensation on the Financial Performance of Listed Commercial Banks in Kenya

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Abstract: **This study examined the effect of executive compensation on financial performance among listed commercial banks in Kenya. The study adopted descriptive research design. The target population comprised of the eleven commercial banks listed at the Nairobi securities exchange as at December 2017 as indicated in CMA bulletin 2017. The study employed secondary data extracted from audited financial statements and annual reports of individual listed commercial banks over the 6-year period, 2012 to 2017. STATA was used to tabulate and analyze the data. Percentages, means and frequency distribution tables were used to describe the data. Relationships between the independent and dependent variables were established by means of regression. The study established that executive annual bonuses, executive fixed salaries, executive allowances had a positive effect on financial performance of listed commercial banks while executive share ownership had a negative effect on the financial performance of the listed commercial banks in Kenya. However, the effect of all the four independent variables including; annual bonuses, executive fixed salaries, executive allowances and executive share ownership did not show statistically significant influence on financial performance of listed commercial banks in Kenya. The study thus concludes that executive compensation does not have a significant influence on financial performance listed commercial banks in Kenya. The study recommends that top management of listed commercial banks in Kenya should improve on executive compensation even though it may not improve financial performance that much.**

Keywords: **Executive Compensation, Financial Performance, Listed banks.**

I. INTRODUCTION

Executive compensation has been an ever ending highly controversial issue in most parts of the world especially Europe and USA. There are a lot of factors that interplay to influence the performance of firms. Executive remuneration is one of the major factors that can have an effect on firm performance (Ayodele, 2012). Often, investigations are hardly made to unravel how the top executives that direct the affairs of a company should receive remuneration and other forms of compensations and incentives. Hence Adeoti and Isiaka (2006) argued that the objective of executive remuneration is to attract, motivate and retain good people for attainment of the organizational performance. Executive compensation which is interchangeably used with executive pay or remuneration comprises of salary and incentive pay. Incentive pay could consists of cash and non-cash packages, and is an aspect in finance and accounting that is yet to gain ascendancy in research especially in developing countries like Kenya. In the Kenyan banking sector, executive remuneration has not come under massive spotlight perhaps due to the nature of executive compensation. As opposed to compensation in the more developed markets, executive compensation in Kenya appears to be limited to cash salary, allowances and cash bonuses as indicated in the various annual reports of listed banks. Further, almost all listed banks apply return on assets as a performance measures Musyoka (2011) , hence, it is fair to conclude that some of the key benchmarks used to set the goals of the executive performance are accounting based and thus the relationship between compensation and accounting based performance measures are likely to be more meaningful. Different mechanisms of mitigating agency conflict have been in existence for many years but using executive compensation has been the greatest puzzle for many financial

analysts, researchers and shareholders at large and whose relationship which is ideally expected to be directly related to their output has proved to be otherwise. In the recent years Kenya have experienced major failures in the banking industry. On 14th August, 2015, Central bank of Kenya (CBK) announced that Dubai bank had failed, and it cited a number of causes for the move to close the bank and causes cited were: deteriorating cash reserve ratio position and failure to honor financial obligations, including Sh48 million due to Bank of Africa Kenya, violations of banking laws and regulations, including failure to maintain adequate capital and liquidity ratios as well as provisions for non-performing loans and weak corporate governance structures which was seen to be the major cause of the bank to collapse. In October 2015, the Central Bank of Kenya (CBK) put another Kenyan bank Imperial Bank, under statutory management. The regulator revealed it had taken the drastic decision after learning that unsafe and unsound business conditions to transact business existed in the bank. Also it appears that following an extended audit tussle, Chase Bank collapsed on the 7 of April. The blame was pointed towards poor governance of the bank, to illustrate the severity of these governance issues, the bank made large amount of loans to its directors, an average of ksh 1.35 billion per director. Therefore in this case a question arised as to how could a SME bank, allow its directors to lend tens of millions of shilling to themselves? It can therefore be said that some of this bank failures is as a result of executive staff behavior like giving themselves high loans which they never repay or even been involved in some fraud activities. However on the other hand several studies carried out by various scholars failed to produce evidence of how compensation is connected or related to performance, Aduda (2011) found a statistically negative non-significant relationship between executive compensation and performance of commercial banks in Kenya. Fernandez (2005) found out that company performance is not significantly related to executive compensation and therefore this shows that these scholars do not agree with the fact that compensation of executives adds any value to the firm. Also other studies have been carried out by different scholars to point out some of the major financial crises that have occurred globally like in the case of Enron, Lehman Brothers and WorldCom according to Frey & Osterlor (2007) whereby they studied the causes of those multinational firms collapsing like poor management of funds by executives bringing about the most major financial crises to have ever occurred, none of the studies carried out focused on the problems that Kenyan financial institutions like banks face which makes them end up collapsing. This study therefore sought to carry out a study on how executive compensation in terms of ownership, allowances, bonuses and salaries positively or negatively affect the financial operations and performance of commercial banks in Kenya, and how better executive compensation can reduce major problems that may affect commercial banks in Kenya.

1. Objective of the Study

The main objective of the study was to determine the effect of executive compensation on the financial performance of listed commercial banks in Kenya. Specific Objectives includes the following:

i. To assess the effect of executive share ownership on the financial performance of listed commercial banks in Kenya.
ii. To determine the effect of executive allowances on the financial performance of listed commercial banks in Kenya.
iii. To examine the influence of executive annual bonuses on the financial performance of listed commercial banks in Kenya.
iv. To establish the effect of executive fixed salary on the financial performance of listed commercial banks in Kenya.

II. LITERATURE REVIEW

1. Theoretical Review

The first theory supporting the study is Agency Theory advanced by Jensen and Meckling (1976). They define an agency relationship as a contract under which one or more persons (the principal) engage another person (the agent) to perform some service on their behalf. A large business can be very difficult to manage without separating the ownership and management because they often have thousands of shareholders and it is impossible for all of them to be actively involved in the management. The authority is therefore often delegated to professional managers, hired by the firmThe Principal-Agent Theory is based on the relationship between shareholder and management, in which the shareholder employs the managers to perform a taskThe separation of ownership and management creates a clear advantage because the share ownership is allowed to change without interfering with the operations of the business However, it can also result in problems. According to Jensen and Meckling (1976), members of the management team are the agents and equity investors (shareholders) are the principals, who may have different motives to run the company. It is assumed that if the

agents and principals are left alone, there is a good probability that each of them would prefer to act in his or her self-interest. In a corporate environment, shareholders want managers to increase the value of the firm, but managers may strive to maximize their own value at the shareholders' expense. Conflicts between shareholders' and managers' objectives are referred as principal –agent problems. In order to reduce divergences of interests, shareholders can establish appropriate incentives for the managers and then monitor their behavior (Jensen and meckling, 1976. p 380). A well-established incentive program can motivate managers to satisfy the shareholders' interest. The disadvantage of this is that creating incentives and monitoring managers is very complicated and costly. These costs are often referred as agency costs and consist of the sum of the monitoring costs of the shareholders and the costs of implementing control devises. In a corporate environment, managers and shareholders also have different information available (Akerlof and Spence, 2001). This means that there are information asymmetries that need to be recognized in order to resolve a principal –agent problem. However, principal –agent problems can never be solved perfectly, which means that shareholders will always experience some losses. These losses are called residual losses according to Jensen and meckling (1976). Therefore in this case executive staffs were to be well compensated by making them own some number of shares, and also given some incentives like allowances and also given some bonuses so that they are motivated to perform and make decisions that benefit the shareholders as well as the company.

The second theory supporting the study is Equity Theory proposed by Stacy Adams (1960s), developed equity theory and they asserted that employees seek to maintain equity between the inputs that they bring to a job and the outcomes that they receive from it against the perceived inputs and outcomes of others (Adams, 1963). Equity theory focuses on determining whether the distribution of resources is fair to both relational partners. Equity is measured by comparing the ratio of contributions (or costs) and benefits (or rewards) for each person. The belief is that people value fair treatment which causes them to be motivated to keep the fairness maintained within the relationships of their co-workers and the organization. The structure of equity in the workplace is based on the ratio of inputs to outcomes. Inputs are the contributions made by the employee for the organization. Boivie, Bednar and Barker (2015) says that what is most desirable about equity theory in terms of explaining executive compensation is that equity theory has been applied at both the individual and team levels of analysis. Equity theory offers predictions about how individuals react to over-reward and under-reward situations. Gomez, Makri and Larraza (2003) confirm that equity theory has played a predominant role in traditional compensation theory and practice. Criticism has been directed toward both the assumptions and practical application of equity theory. Scholars have questioned the simplicity of the model, arguing that a number of demographic and psychological variables affect people's perceptions of fairness and interactions with others. Furthermore, much of the research supporting the basic propositions of equity theory has been conducted in laboratory settings, and thus has questionable applicability to real-world situations (Huseman, Hatfield & Miles, 1987). Critics have also argued that people might perceive equity/inequity not only in terms of the specific inputs and outcomes of a relationship, but also in terms of the overarching system that determines those inputs and outputs. Thus, in a business setting, one might feel that his or her compensation is equitable to other employees', but one might view the entire compensation system as unfair (Carrell & Dittrich, 1978). According to equity theory, individuals make subjective assessments of the ratio of their inputs (effort) and outcomes (compensation) to those of referent others, and experience dissonance when the Relationship between Long-Term Incentives and Corporate Performance. Gerakos, Ittner and Moers (2013) assert that employees seek to maintain equity between the inputs they provide and the outputs they receive in comparison to the perceived inputs and outputs of others. The theory thus suggested that executive directors were more aggressive in performing best if they feel that the rewards they get, like been paid high salaries and been allowed to own some shares measure up to the performance they bring and thus this increases the financial position of the company.

2. Empirical Review

Executive Share Ownership and Financial Performance: Anderson (2000) carried out a study in the United States by investigating executive share ownership for a period 1997 to 1999 and the study was based on quantitative method. He found out that managerial ownership in banks is positively related to greater firm financial performance and thus he concluded that the executive share ownership should be given a priority because it have an effect on the overall financial performance of a bank Westman (2014) also carried out a similar study in Europe for a period 2001 to 2002 whereby he uses quantitative method and he found that managerial ownership had a negative impact on the banks' performance during the recent financial crisis. Specifically, he found a positive impact of management ownership in small diversified banks and non-traditional banks, the monitoring of which is challenging due to their capacity.

K'obonyo (2011) in a census study in Kenya examine the interrelations among ownership structure and firm performance measured using accounting based measures amongst all firms listed at the NSE for a period between 1998-2010. The study is informed by the proposition that insider ownership is actualized through executive share options. The findings suggest a positive relationship between insider ownership and firm performance thereby affirming the proposition that when managers own shares, they become more committed to the organization since they have a stake in the residual income of the firm and they are likely to bear the costs of mismanagement.Related to bankers' compensation in form of share ownership, Fraser (2000) found that managerial ownership in banks is positively related to good performance, but that this relationship became negative in conjunction with regulatory changes in the United States around 1990, Fraser used quantitative method in carrying out his study. Ongore (2011) carried out a study using quantitative method about share ownership in Kenya and in his study the shareholders have the power and incentive to closely monitor the performances of the management. This in turn has two consequences in relation to firm performance. Close monitoring of the management can reduce agency cost and enhance firm performance. On the other hand, concentrated ownership can create a problem in relation to overlooking the right of the minority and also affect the innovativeness of the management. On my take I suggest that executive staff should be allowed to own some number of shares for themselves so that they can feel as part of the company they work for, and that made them make decisions that positively increase the value of the company the work for.

Executive Allowances and Financial Performance: Hubbard and Palia (2001) carried out a study in 60 large UK firms using quantitative method within the period 1998-1999 in the study they investigated the relationship between allowances offered to executive staff and how it affects the financial performance. The outcomes of their findings show that the inclusion of executive allowances significantly increases the performance of any company and that is because executive staffs are willing and motivated to work for the best good of the company and the shareholder as well.

Doucouliagos (2007), examine the relationship between director allowances given and performance within Australian banking using panel data covering the periods of 1992 -2005. The outcome of their work revealed the existence of a positive relationship between CEO remuneration and bank performance he used quantitative method in his study. Haid (2006) in his study carried out an investigation by analyzing the relationship between financial perfomance and executive compensation in Germany using a sample of large listed German firms between the periods of 1987 to 2003 using both qualitative and quantitative method. The results of his findings indicate that level of executive compensation in terms of allowances allocated and financial performance is weaker in firms. Ampuero, (2009) in his research examines the relationship between allowances compensation and company performance within the banking sector, using a sample of twelve banks involving Swedish and foreign banks in Sweden covering 2006 to 2008 and adopting a combination of qualitative and quantitative method, the outcome of his findings shows that only turnover shows a significant p-value while other variables like bonuses and allowances and also salaries are not related to financial performance.

Executive Annual Bonuses and Financial Performance: Bruce, Skovoroda, Fattorusso and Buck (2007), carried out a study on executive bonuses and firm performance in the U.K. by investigating executive bonuses for the period 2001 to 2003 using quantitative method. Their main finding demonstrated that executive bonuses are related to higher total shareholder returns. Crumley (2008) examined the relationship between firm performance and CEO compensation in the U.S. commercial banking industry using quantitative method. The sample of his study covered 36 firms in the U.S commercial banking industry for the period between 2002-2003. His results exhibited a weak relationship between CEO remuneration and firm performance. Armstrong and Vashishtha (2012), carried out a study in the United States for a period 2007-2008 using quantitative method and there is empirical evidence on the impact of bonus of top organizational leadership on financial performance, their study show that the higher the bonus the higher the performance which demonstrate managerial effectiveness. Han and Shen (2007) examined the relationship of performance based bonus on employee's and performance efficiency in China for a period between 2004-2005 using both qualitative and quantitative method. The study found strong correlations and therefore concluded that commensurate bonus payment increases employee efficiency and innovativeness thereby decreasing the operational gaps. Fahlenbrach and Stulz (2011), show that banks with higher option compensation and a larger fraction of compensation in cash bonuses for their CEOs did not perform worse during the crisis in the United States. Further, banks with higher option compensation and with a larger fraction of compensation given in the form of cash bonuses did not have worse performance during the crisis. The incentives of non-CEO top executives are unrelated to bank performance during the crisis. Bank CEOs did not reduce their holdings of shares in anticipation of the crisis or during the crisis; there is also no evidence that they hedged their equity exposure. Consequently, they suffered extremely large wealth losses as a result of the crisis

Executive Fixed Salary and Financial Performance: Conyon, Main, Bruce and Benito (2000), carried out a study regarding executive salaries in a UK firm for a period 1996-1998 using quantitative method and they realized that there is a little relationship between these variables and thus confirmed low pay-performance sensitivities. Fernandes, Ferreira, Matos and Murphy (2009), report that the positive relationship between CEO pay and firm size documented in the U.S. for a period 2006-2007 using quantitative method is pervasive across all countries, although the pay-size elasticity is higher in the U.S. than elsewhere. Lishenga (2011) applies a comparative study to investigate the sensitivity of corporate governance structures and practices to performance declines amongst companies quoted on the NSE for the period of eight years from the beginning of 1998 through 2005 in Kenya. Components of corporate governance such as CEO compensation measured as salaries, board composition, CEO and insider equity holdings, and frequency of board meetings are studied with reference to the financial performance of the firms classified in cohorts of losers, winners and mixed. The study employs the Tobin‘s Q as proxy for financial performance and concludes that insider ownership falls with falling firm performance as CEO remuneration is insensitive to firm performance. In Kenya, Gathua, Ngumi and Kiragu (2013), examined the relationship between executive compensation and financial performance among commercial banks in Kenya for a period between 2009-2011 using quantitative method, the study found that executive compensation has insignificant relationship with financial performance among commercial banks in Kenya. Performance was measured by use of non-performing loans, money laundering, creative accounting and dividend pay-out. A further study to establish the determinants of executive compensation among commercial banks in Kenya is therefore recommended. The management of commercial banks should continue to enhance controls within operational areas that can pose a risk to the bank. Management actions should continue to be reviewed to ensure that they do not affect the banks business adversely. Conyon and He (2016) examined the relationship between CEO compensation and corporate fraud in China, the study found a correlation between executive compensation and fraud, the lower the executive compensation the higher the incidences of fraud. Conyon and He (2016), studied the effect of executive remuneration, the study found that fixed pay tend to decrease after enforcement action by China Securities and Regulatory Commission.

III. METHODOLOGY

This study adopted a descriptive research design. According to Mugenda and Mugenda, (2003), descriptive research is a process of collecting data in order to test hypotheses or to answer questions concerning the current status of the subjects in the study. The target population comprised of the eleven commercial banks listed at the Nairobi securities exchange as at December 2017 as indicated in CMA bulletin 2017. Since the target population comprised 11 commercial banks listed in NSE, a census of all the firms study was conducted for the study. According to Mugenda and Mugenda (2003), a census is preferred where the population is small and manageable. Further, census method enhances validity of the collected data by eliminating errors associated with sampling (Saunders, Lewis, & Thornhill, 2009). The study employed secondary data that were be extracted from audited financial statements and annual reports of individual listed commercial banks over the 6-year period, 2012 to 2017. Collection of data was accomplished by means of the secondary data collection instrument. The instrument that aided in collection of data relating to executive share ownership, executive fixed salary, executive allowances, and executive annual bonuses were collected. Using the data collection instrument, the information on specific components was keyed in for each firm for every year. In order to verify the authenticity of the collected data, the same was cross-checked by using the hand book summaries obtained from NSE website for the period of study. The data was then uploaded in Excel program and converted into ratios. The ratios were then converted into panels ready for analysis.

Data analysis is a practice in which raw data is ordered and organized so that useful information can be extracted from it (Saunders, 2011). STATA was used to aid in data analysis. Descriptive Statistics was used in transforming the raw data into a form that can easily be understood and interpreted. The first form of analysis involved computation of averages, frequency distributions and percentage distributions (Adejimi, Oyediran & Ogunsanmi, 2011). Descriptive statistics such as, mean and frequencies was used to perform data analysis. Descriptive statistics was used to derive conclusions and generalizations regarding the population. The mean scores was used to rate the factors, share ownership, executive fixed salary, executive allowances and executive annual bonuses in order of their importance. Standard deviation of each of the factors will be calculated to measure the variability of the responses. Panel data, which is also known as longitudinal or cross-sectional time-series data, is a dataset in which the behavior of entities is observed across time, these entities could be states, companies, individuals or countries. Panel data is derived from a usually small number of observations over time on a usually large number of cross-sectional units like firms or governments (Moffatt, 2017). Model specification involved coming up with a combination of study variables that represented the empirical relationship between the dependent and explanatory variables.

$$Yit = \alpha + \beta 1X1it + \beta 2X2it + \beta 3X3it + \beta 4X4it + \mu it \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (1)$$

Where: Yit =financial performance, α = the Y intercept; $X1it$= executive share ownership; $X2it$= executive allowance, $X3it$= executive annual bonuses, $X4it$= executive fixed salary and μit= error term which is assumed to be normal in distribution with mean zero and variance Multicollinearity was assessed in this study using the variance inflation factors (VIF). According to Field (2009) VIF values in excess of 10 is an indication of the presence of Multicollinearity. **Panel Unit Root Test:** Unit root tests was conducted using the Levin, Lin and Chu Statistics (LLC) at 5% level of significance to establish whether the variables are stationary or non-stationary. The purpose of this was to avoid spurious regression results being obtained by using non-stationary series. **Testing Heteroscedasticity:** Modified Wald test was used to test for heteroskedasticity. The null hypothesis in the test is that error terms have a constant variance (i.e. should be Homoskedastic) at 5% significance levels. **Testing Normality:** Jarque-Bera test which is a more conclusive test than the graphical method was conducted. The null hypothesis under this test is that the disturbances were not normally distributed. If the p-value is less than 0.05, the null of normality at the 5% level was to be rejected. **Autocorrelation:** To cater for serial correlation, the Woodridge test for autocorrelation was employed. Serial correlation is a common problem experienced in panel data analysis and has to be accounted for in order to achieve the correct model specification. According to Wooldridge (2003), failure to identify and account for serial correlation in the idiosyncratic error term in a panel model may result into biased standard errors and inefficient parameter estimates. The null hypothesis of this test is that the data has no serial correlation tested at 5% level of significance. **Hausman Test:** Hausman test was done (Stephanie, 2017). The Hausman test is sometimes described as a test for model misspecification. In panel data analysis, the Hausman test can help one to choose between fixed effects model and a random effects model. The null hypothesis is that the preferred model is random effects; the alternate hypothesis is that the model is fixed effects. Essentially, the test looks to see if there is a correlation between the unique errors and the regressors in the model. The null hypothesis is that there is no correlation between the two. Interpreting the result from a Hausman test is straightforward whereby if the p-value is small (less than 0.05), reject the null hypothesis.

IV. RESULTS AND DISCUSSIONS

1. Descriptive Analysis

Results in table 1 below indicate the summary descriptive statistics of executive compensation and financial performance of listed commercial banks in Kenya.

Table 1: Summary Statistics of Executive Compensation and Financial Performance

Variable	Obs	Mean	Std. Dev.	Min	Max
Executive share ownership	66	0.0412	0.0713	8.37E-06	0.2057
Executive Allowance	66	0.0123	0.0154	0.0006	0.0973
Executive annual bonuses	66	0.0418	0.0327	0.0040	0.1380
Executive Fixed salary	66	0.0056	0.0078	0.0008	0.0381
Financial Performance	66	0.0451	0.0171	-0.0134	0.077

Results in table 1 below indicate the summary descriptive statistics of executive compensation and financial performance of listed commercial banks in Kenya.

The mean for Financial performance was Mean of 0.0451, executive share ownership in relation to total shareholding had a mean of 0.0412 while executive fixed salary in relation to total operating expense posted a mean of 0.0056, results also indicated that executive allowance in relation to total operating expense had a mean of 0.0123 and finally executive annual bonus to total operating expense mean was 0.0418. The Std. Dev. for Financial Performance was 0.0171, the standard deviation for executive share ownership to total shareholding was 0.0713, executive fixed salary to total operating expense had a standard deviation of 0.0078, standard deviation for Executive Allowance to total operating expense was 0.0154 and finally, the standard deviation for Executive annual bonuses to total operating expense was 0.0327. Executive allowance to total operating expense posted minimum of 0.0006, Executive share ownership to total shareholding had a minimum of 8.37E-06, Executive Fixed salary to total operating expense had a minimum of 0.0008, Financial Performance had a minimum of -0.0134 and results for executive annual bonus to total operating expense had a

minimum of 0.0040. The maximum for financial performance was 0.077, executive share ownership to total shareholding had maximum of 0.2057 while executive fixed salary to total operating expense posted a maximum of 0.0381, results also indicated that executive allowance to total operating expense maximum was 0.0973 and finally executive annual bonus to total operating expense maximum was 0.1380.

2. Correlation Analysis

Correlation coefficient values ranging between 0 and 1 measures the degree to which two variables are linearly related with the higher magnitude indicating higher degree of association between two variables. Adejimi, Oyediran and Ogunsanmi (2011) observed that a correlation coefficient of magnitude 0.3–0.5 shows a medium linear dependence between two variables while 0.5 to 1.0 shows a strong linear dependence.

Table 2: Pearson Correlation

	Executive share ownership	Executive Allowance	Executive Annual Bonuses	Executive fixed salary	Financial performance
Executive share ownership	1				
	66				
Executive Allowance	-0.0873	1			
	0.4857				
	66	66			
Executive Annual Bonuses	-0.2699	-0.1593	1		
	0.0284	0.2012			
	66	66	66		
Executive fixed salary	-0.1288	-0.2066	0.0763	1	
	0.3028	0.0961	0.5428		
	66	66	66	66	
Financial performance	-0.3089	-0.0482	0.414	0.4853	1
	0.0116	0.7006	0.1022	0.000	
	66	66	66	66	66

The correlation results in Table 2 below indicate that executive share ownership was negatively associated to financial performance among listed commercial banks listed in NSE (r= -0.3089, p=0.0116). Similarly, executive allowance was negatively associated to financial performance (r= -0.0482, p= 0.7006). Executive fixed salary was positively associated to financial performance (r= 0.4853, p=0.000). Also, executive annual bonuses had a positive association to financial performance (r= 0.414, p=0.1022).

3. Diagnostic Tests

Multicollinearity Test: The variance inflation factors results and were established to be 2.78 which is less than 10 and thus according to Field (2009) indicates that there is no Multicollinearity. **Panel Unit Root Tests:** Results indicated that all variables are stationary (i.e. absence of unit roots) at 5% level of significance. **Heteroskedasticy Test**: The results indicate that the error terms are homoscedastic, given that the p-value is more than the 5% (0.06),hence the null hypothesis of constant variance was accepted. **Normality Tests**: Given that the majority of p-value were less than 5% for the residual, the null hypothesis is rejected and thus the conclusion that the residuals are normally distributed. **Autocorrelation**: Wooldridge test for autocorrelation was conducted. The null hypothesis is that no first order serial /auto correlation exists. The results are as indicated in Table 4.7 below and therefore the null hypothesis of no autocorrelation is accepted and therefore residuals are not auto correlated (p-value=0.5770). **The Hausman Test for Model Effect Estimation**: The Hausman test was employed to determine the most suitable model for this study. The Chi-square test statistic is 2.93 with an insignificant probability of 0.5697 which means that the null hypothesis is rejected in favor of the. Random effects model. Therefore, we accept the random effects model as suitable for this study. **Regression Analysis.** The regression model helps to explain the magnitude and direction of relationship between the variables of the study through the use of coefficients like the beta coefficient and the level of significance. Based on the diagnostic tests carried out the study adopted a random effect model and the result presented was to show the fitness of model used of the regression model in explaining the study phenomena.

4. Regression Analysis

Table 3: Random Effect Model

R-sq:				Obs per group:		
within = 0.0505			min =		6	
between = 0.2293			avg =		6	
overall = 0.1893			max =		6	
			Wald chi2(4)	=	5.35	
Corr (u_i, X) = 0 (assumed)			Prob > chi2	=	0.2531	
y	Coef.	Std. Err.	z	P>|z|	[95% Conf.	Interval]
x1	-.0562	.0627	-0.90	0.370	-.1791	0.0667
x2	.0936	.0993	0.94	0.346	-.1009	0.2882
x3	.1220	.0734	1.66	0.097	-.0219	0.2659
x4	.4678	.3522	1.33	0.184	-.2225	1.1580
_cons	.0385	.0074	5.18	0.000	.0239	0.0530

Effect of executive share ownership on financial performance : Table 3 shows the effect of executive share ownership on financial performance. The researcher wanted to test the null hypothesis that Executive share ownership has no significance on the financial performance among the listed commercial banks in Kenya. Using random effect model. It was established that Executive share ownership had a statistically insignificant effect on financial performance ($\beta 1 = -.0562$, $p = .370$ and $\alpha = 0.05$). Hence the study failed to reject null hypothesis . The insignificant effect could be explained by the fact that share ownership by management may lead to greater risk taking that may plunge the bank into financial performance problems since the mangers loses their objectivity in chase of risky projects that may translate to poor performance.The insignificant relationship should be expected since studies done by other researchers reveal similar results. Westman (2014) also carried out a similar study in Europe for a period 2001 to 2002 whereby he uses quantitative method and he found that managerial ownership had a negative impact on the banks' performance during the recent financial crisis. however K'obonyo (2011) finds contrary results in a census study in Kenya examine the interrelations among ownership structure and firm performance measured using accounting based measures amongst all firms listed at the NSE for a period between 1998-2010. The study is informed by the proposition that insider ownership is actualized through executive share options. The findings suggest a positive relationship between insider ownership and firm performance thereby affirming the proposition that when managers own shares, they become more committed to the organization since they have a stake in the residual income of the firm and they are likely to bear the costs of mismanagement.

Effect of executive allowance on financial performance : Table 3 shows the effect of executive allowance on financial performance .The researcher tested the null hypothesis that Executive allowance has no significance on the financial performance among the listed commercial banks in Kenya. Results show that executive allowance had a statistically insignificant effect on financial performance of listed commercial banks ($\beta 2 = .0936$, $p = .346$ and $\alpha = 0.05$). The study therefore fails to reject null hypothesis .The insignificant effect could be attributed to that fact that financial compensation like allowances may not motivate the executive directors to improve their over sight role in prudential management of commercial banks since their motivating effect is short lived. The study is in agreement with prior studies. Doucouliagos (2007), examine the relationship between director allowances given and performance within Australian banking using panel data covering the periods of 1992 -2005. The outcome of their work revealed the existence of a positive relationship between CEO remuneration and bank performance he used quantitative method in his study. Haid (2006) in his study carried out an investigation by analyzing the relationship between financial perfomance and executive compensation in Germany using a sample of large listed German firms between the periods of 1987 to 2003 using both qualitative and quantitative method. The results of his findings indicate that level of executive compensation in terms of allowances allocated and financial performance is weaker in firms. Ampuero, (2009) in his research examines the relationship between allowances compensation and company performance within the banking sector, using a sample of twelve banks involving Swedish and foreign banks in Sweden covering 2006 to 2008 and adopting a combination of qualitative and quantitative method, the outcome of his findings shows variables like bonuses and allowances and also salaries are not related to financial performance.

Effect of Executive annual bonuses on financial performance: The null hypothesis Executive annual bonuses has no significance on the financial performance among the listed commercial banks in Kenya .The findings show that Executive annual bonuses had a statistically insignificant effect on financial performance of listed commercial banks in Kenya ($\beta 3 = .1220$, $p = .097$ and $\alpha = 0.05$).The null hypothesis was thus not rejected. The possible explanation for this insignificant effect is that improved annual bonuses being related to annual performance of the bank and being tied to performance of the bank may motivate the top management of the respective banks to be prudent enough and mange efficiently to improve performance such that they can receive higher allowances at the end of financial year. However, the effect was not statistically significant meaning there are other major determinants of financial performance of commercial banks and that financial compensation may not necessary motivate executive much. The finding is in agreement with other studies like Bruce, Skovoroda, Fattorusso and Buck (2007), carried out a study on executive bonuses and firm performance in the U.K. by investigating executive bonuses for the period 2001 to 2003 using quantitative method. Their main finding demonstrated that executive bonuses are related to higher total shareholder returns. Crumley (2008) examined the relationship between firm performance and CEO compensation in the U.S. commercial banking industry using quantitative method. The sample of his study covered 36 firms in the U.S commercial banking industry for the period between 2002-2003. His results exhibited a weak relationship between CEO remuneration and firm performance. Armstrong and Vashishtha (2012), carried out a study in the United States for a period 2007-2008 using quantitative method and there is empirical evidence on the impact of bonus of top organizational leadership on financial performance, their study show that the higher the bonus the higher the performance which demonstrate managerial effectiveness. however study by Fahlenbrach and Stulz (2011), finds contrary results that banks with larger fraction of compensation in cash bonuses for their CEOs did not perform worse during the crisis in the United States. Further, banks with higher option compensation and with a larger fraction of compensation given in the form of cash bonuses did not have worse performance during the crisis.

Effect of executive fixed salaries on financial performance: Using panel regression analysis, it was established that executive fixed salaries had a statistically insignificant effect on financial performance ($\beta 4 = .4678$, $p = .184$ and $\alpha = 0.05$).The null hypothesis was not rejected. The effect can be attributed to the fact that when banks offer more absolute fixed salaries to executive at any particular time, they are motivated to be practice prudential management however; the effect was not statistically significant due to the fact that a mare increase in fixed salaries does not necessarily mean the bank will translate such heavy payment as shown by fact that when directors get higher fixed salaries, they may reduce time to board meetings to attend personal investments. Other studies also show similar results. study by Conyon, Main, Bruce and Benito (2000), carried out a study regarding executive salaries in a UK firm for a period 1996-1998 using quantitative method and they realized that there is a little relationship between these variables and thus confirmed low pay-performance sensitivities. Study by Lishenga (2011) concludes that CEO remuneration is insensitive to firm performance. In Kenya, Gathua, Ngumi and Kiragu (2013) found that executive compensation has insignificant relationship with financial performance among commercial banks in Kenya. Conyon and He (2016) examined the relationship between CEO compensation and corporate fraud in China, the study found a correlation between executive compensation and fraud, the lower the executive compensation the higher the incidences of fraud. Conyon and He (2016), studied the effect of executive remuneration, the study found that fixed pay tend to decrease after enforcement action by China Securities and Regulatory Commission.

V. CONCLUSION

The study concludes that Executive Share Ownership does not have a significant influence on financial performance of listed commercial banks in Kenya. The study finds a negative insignificant relationship between financial performance and executive share ownership. That means even if banks increase directors share ownership it will not have any effect on financial performance. The study therefore concludes that the effect of executive share ownership was weak. The study therefore concludes that executive share ownership may not necessarily lead to improved financial performance of listed commercial banks in Kenya. Based on the findings that the effect of Executive annual bonuses had a statistically insignificant positive effect on financial performance of listed commercial banks in Kenya. The study concludes that that executive annual bonus contributes marginally to financial performance. Any improvement of executive annual bonuses should lead to improved financial performance. However, the insignificant effect could be attributed to that fact that financial compensation like allowances may not motivate the executive directors to improve their performance level and that of the company.

Based on finding that executive allowance had a statistically insignificant positive effect on financial performance of listed commercial banks. The study concludes that any improvement in executive allowance to executive directors may translate to financial performance of listed commercial banks. However, the effect was too marginal as evidenced by the statistically insignificant influence. The management may decide to improve the allowances of the executive directors to protect them from the economic challenges hence make them motivated in their oversight role of the operations of the banks through various committees if the banks management. However, the increase in the annual allowances may not necessarily lead to major improvement in profits of the listed commercial banks. Finally, based on the finding that executive fixed salaries had a statistically insignificant positive effect on financial performance of listed commercial banks, the study concludes that any improvement in fixed salaries offered to executive directors leads to increased financial performance through improved oversight and supervisory role. However, the effect was marginally and weak as evidenced by insignificant effect. The bank management may decide to improve the fixed salaries of executive managers but that may not necessarily translate to improved financial performance.

Based on the conclusions, a number of recommendations are made. The management of listed commercial banks in Kenya should not increase the stock ownership of executive managers as this may lead to greater risk taking that may plunge the bank into financial performance problems since the mangers loses their objectivity in chase of risky projects that may translate to poor performance. The increase in executive share ownership should thus be controlled. Secondly, based on the conclusion that executive annual bonuses have positive effect on financial performance. The study recommends to the top management of the listed commercial banks to consider improving the annual bonuses given to executive managers. However, the bonuses should not be given much weight, as their effect on financial performance is a weak one. Thirdly, based on the findings that executive annual allowances have a positive effect on financial performance of listed commercial banks in Kenya, The study wishes to recommend to top management of the listed commercial banks to improve the annual allowances offering to executive directors. The top management of the listed commercial banks should consider improving the annual allowances to enhance financial performance of the listed commercial banks. Finally, the study wishes to recommend to the top management of listed commercial banks to consider improving the fixed salaries of executive directors of the bank. The study however does not place much emphasis on the fixed annual salaries as this may not necessary lead to major increase in financial performance of the listed commercial banks in Kenya. The current study sought to establish the effect of executive compensation on financial performance of listed commercial banks. The study was successfully carried out, however a number of gaps were identified that should form gap for future studies. First, a similar study should be done with improved model. The model of analysis should introduce control variables into the analysis especially the bank specific factors to improve the robustness of the estimation model. Additionally, another study should be carried that considers all the commercial banks in Kenya. Lastly, the same study could also be carried out in the deposit taking Sacco's to observe if the results are holding.

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