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## The Moderating Effect of Strategic Leadership on the Relationship between Executive Compensation and Performance of Commercial Banks in Kenya

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### Abstract

Boards of Directors are not only held responsible for an organization's failure to conform to rules and regulations or failure to attain organizational performance goals, they are also supposed to remunerate and monitor company management's performance. The purpose of this study was to examine the moderating effect of Strategic leadership on the relationship between executive compensation and the performance of commercial banks in Kenya. The specific objectives of this study were: to establish the influence of Share ownership on the performance of commercial banks in Kenya; to determine the influence of Executive perks on the performance of commercial banks in Kenya; to determine the relationship between Bonus payment and performance of commercial banks in Kenya; to examine the extent to which strategic leadership moderates the relationship between executive Compensation and the performance of commercial banks in Kenya. This study was anchored on Contingency theory and Stewardship theories. The research design for the study was correlational design. The target population was all operational registered commercial banks in Kenya which are thirty-nine (39) in number; the sample size was obtained using purposive sampling technique where the respondents were the Chief Executive Officers (CEOs) of each bank and one executive director for each bank giving a total sample size of 78. Data was collected using questionnaires. Ordinal logistic regression analysis was performed on the data collected using R technique to estimate and provide empirical evidence on the nature of relationship between compensation system and bank performance. The research hypotheses were tested by determining the significance of the regression coefficients of the estimated models. Share ownership was found to have a positive and significant relationship with the performance of commercial banks in Kenya; payment of executive perks was found to have a positive and significant relationship with the performance of commercial banks in Kenya, embracing strategic leadership by the board was found to positively influence the relationship between executive compensation and the performance of commercial banks in Kenya. Based on the findings, the study recommends that; Banks should establish a system of compensation that is performance based and top executive should be allowed share ownership of these banks, this will induce the top management to align their interests to the interest of these banks and subsequently work to improve the performance of these banks; Banks should pay competitive executive perks to the top management as a way of motivating good performance; Banks Boards of Directors should offer strategic leadership by drawing strategic plans detailing clear strategic objectives on key areas of operation, disseminate the same to all bank employees with the view to having them buy in and direct their efforts to areas that are productive. Banks should employ people with strategic orientation especially at the top-level management and invest resources in developing capacity for strategic leadership.

**Keywords:** Executive compensation, firm performance, stewardship theory, strategic leadership

## 1. Introduction

### 1.1. Background

Firm performance as a result of corporate governance has received enormous attention in economic, finance and management literature in recent years. The motivation behind this attention has been the scandals that rocked the U.S. economy in early and late 2000 and the Asian financial crisis of late 90s. Failures in the corporate reporting process has been cited as the reason behind the fall of high profile companies in the USA, UK and other parts of the world (IFAC, 2003). Apart from signaling the largest corporate bankruptcy in the USA, the failure of Enron Corporation in late 2001, also raised a myriad of questions about the effectiveness of contemporary auditing, accounting, and Corporate Governance practices (Vintern, 2002). The Enron scandal which occurred in early 2000 led to the reduction of its market value from US\$ 80 billion in August 2000 to less than US\$ 1 billion in 2001 when the scandal was unearthed. The quality of corporate

governance regimes is what institutional investors rely on in making decisions, and place a cost (a financial premium) where systems are weak. Promotion of good corporate governance contributes positively to the development of both national capital markets and promotion of foreign direct investment. Thus, the significance of corporate governance is now widely recognized both for national development, and as part of the international financial architecture. In the words of the President of the World Bank: "The proper governance of companies will become as crucial to the world economy as the proper governance of countries" (Godfrey, 2002).

Godfrey (2002) posits that in addition to the South African King Report, there has been a rapid growth in the development of African thinking on corporate governance. New thinking is to attack on the supply side of corruption (company bribes) by complementary anti-corruption measures by the state. The recent initiative of the African Union (AU) to develop an AU Convention on Combating Corruption addresses the importance of declaring public officials' assets, and also breaks ground by targeting unfair and unethical practices in the private sector. Corporate governance is now established as an important component of the international financial architecture, but barely half a decade ago it was little known beyond specialists in a few countries such as the US, the UK, Australia, Canada and South Africa. According to Elewechi (2007) there has been an increase of initiatives by Reserve Banks and Central Banks alongside other institutions worldwide such as the Organization of Economic Cooperation and Development (OECD) and the Basel Committee on Banking and Supervision to provide governance principles with a view of tightening and enhancing management and performance of the banking industry which is an important sector in any economy.

### 1.2. Executive Compensation

Executive compensation according to Maijor and Vanstraelen (2006) is the pay given to an officer at the top level management of a company, which is basically a mixture of monthly salary, shares of or call options on the company stocks, bonuses, benefits, and perquisites, basically designed to take into account tax laws, government regulations, organizational desires and the executive, and rewards for performance.

Scholars in the area of Corporate Governance have long given attempts to understand a myriad of underpinning factors of executive compensation. Agency theory giving the most popular stream of research which suggests that performance-based incentives and constituting of Boards of Directors are simply among the most important governance mechanisms that facilitate reduction of executives' opportunistic behavior and makes them align their interests with those of shareholders (Tosi, et al., 2000).

Wilkinson (2009) posits that under the right circumstances, organizations that pay their top management the right rewards should outperform their peers. It has however been argued that even if performance-related, short-termism in remuneration packages to company executives, were somewhat responsible for the global economic crisis, which resulted from the collapse of the market capitalization of the United States banks (Bebchuk & Spamann 2010; Fahlenbrach & Stulz 2011). Brick, Palmon and Wald (2006) however argue that employees who are strongly motivated by money and personal gains are likely to be tempted to commit fraud.

According to Colvin (2008) any form of executive compensation should translate to the performance of an organization, because many company chief executive officers (CEOs) are often paid excessively in the form of share options, despite their organizations' financial challenges. Chinese investors protested when they received reports which indicated that senior executives of loss-making companies rewarded themselves with hefty general compensation packages (Xiaoning 2009). In his study, De Wet (2013) found that similar protests and objections against excessive executive compensation had been heard from across the world. The Kenyan situation is unfortunately no exception.

Since 1990s, the practice of equity-based compensation has doubled and is still growing. The motivation behind incorporating equity in the executive compensation package is to induce and motivate corporate managers to only engage in activities that will take care of and maximize shareholders' wealth. Murphy (2012) asserts that executives note the opportunity to increase their wealth with the increase in stock returns when they are given the opportunity to become part-owners of the company. As a result, corporate executives will engage in activities that will boost the performance of the company thus leading to performance increase in stock price. This price increase will make executives cash in large compensation. Scholars have undertaken studies on the relationship between incentive compensation and the company performance using several measures. Among them, the pay-volatility sensitivity and the pay-performance sensitivity which are the two most important measures of CEO incentive in the literature (Murphy 2012).

### 1.3. The Concept of Strategic Leadership

Strategic leadership according to Carter and Greer (2013) is the ability of the leaders of the organization to envision and direct efforts and actions of the organization toward the successful attainment of the organizational objectives. The failure to achieve profitability targets by most organizations is due to limited exposure and experience to strategic leadership (Carmeli et al., 2011). Strategic leadership Knowledge is crucial for the top management teams because the demands from shareholders and stakeholders have increased in both complexity and intensity (Carter & Greer., 2013). A lack of orientation to the work of strategic leadership may jeopardize organizational performance, organizational competitiveness, and sustainability (Bansal & Desjardine, 2014).

Kjelin (2009) defines Strategic leadership as the ability of firms to envision, anticipate and maintain flexibility, and empower others to create a strategic opportunity and a reliable future of the organization. Strategic leadership as defined by Guillot (2003) is the ability of, a senior leader who is experienced and has wisdom and vision to make and execute plans and make consequential decisions in the uncertain, volatile, complex and ambiguous strategic business environment. Harrison (2003) indicates that strategies and performance of organizations is purely the responsibility of senior executive management. Just as poor leadership can have a powerful negative influence; excellent leadership can have an enormous

positive influence as well. Business organizations with a perspective approach will have management that has shared view and vision and create a positive impact on the environment where it operates. Therefore, strategy is required to focus effort within the organization and promote coordination of activities. In the absence of strategy, a firm becomes a bunch of individuals, hence strategy is needed to ensure people's collective efforts and concentration of actions towards achieving organizational objectives and plans.

Beck and Wiersema (2013) argue that firm performance is something that hinges on the dynamic capabilities of the management in resourcing of the organization and the strategic decision-making framework employed by the specific organizations. Managerial capabilities are comprised of different managerial competencies that are dynamic and have a significant influence in directing the company's strategy (Tubs & Schulz, 2006).

#### 1.4. Firm Performance

Success is the motivation behind firms' engagement in business. The measurement of this success comes in several ways. The level of success is measured in terms of business performance (Waweru, 2008). In order to measure the extent of success, firms measure among other things profitability using traditional performance measures.

Firm performance according to Lebens and Euske (2006) is a set of nonfinancial and financial indicators that give information on the extent of achievement of organizational objectives and results (Lebens & Euske, 2006). The common performance indicators used are financial performance, operational performance, and overall effectiveness. Overall profitability is the hall mark of financial performance (indicated by ratios such as Return on Investment, return on sales, Return on Assets and Return on Equity), profit margin, earnings per share, stock price and sales growth. Indicators for Operational performance include both product-market outcomes (including efficiency, market share, innovation and new product introduction, and service or product quality) and internal process outcomes like productivity, employee retention, and satisfaction.

In recognition of the vital role the banking sector plays in economic development, there has been an upsurge of initiatives worldwide by Central Banks and Reserve Banks alongside other institutions such as the Basel Committee on Banking and Supervision and OECD to provide governance principles with a view of enhancing management and performance of this important sector. Most of these initiatives have prominently featured in developed nations such as: U.S.A., United Kingdom, Germany, Canada, and France among others with South Africa taking a lead in addressing corporate governance issues among developing nations (Elewechi, 2007).

#### 1.5. Banking Industry in Kenya

In Kenya Commercial Banks accept deposits from individuals and make a profit by using the deposits to give loans to businesses with a high interest rate. For many years now, the subject of corporate governance in Kenya has been top on the agenda by the Regulator. Despite a strong regulatory framework, corporate governance has continued to weaken in Kenya leading to many cases of bank failures as highlighted:

Imperial Bank Limited was established as a Finance and Securities Company in 1992. The year 1996 is when the bank officially began commercial banking services, after being issued with a banking license by the CBK. The bank's stock was privately held. The bank is a medium-sized retail bank that served both corporate clients and individuals as well. By December 2013, the bank's total asset base was valued at about KES 43 billion, with shareholders' equity of approximately KES 5.719 billion. At that time, the bank ranking placed the bank at position nineteen (19) making it the 19<sup>th</sup> largest Kenyan commercial bank, by assets, out of forty-three licensed banks in the country (CBK, 2016).

In October 2015 however the Central Bank of Kenya put Imperial Bank under statutory management. Unsound and unsafe business conditions and practices of transacting business in the bank were the main reasons for Imperial Bank receivership. At the time when the bank was being taken over by KDIC, the bank had about 53,000 customers with deposit estimated at KES 58 billion. NIC Bank was appointed on 21 June 2016, as asset and liabilities consultant for Imperial Bank (while in receivership) by the Central Bank of Kenya. As a result, NIC Bank became responsible for returning funds to imperial bank deposit customers. NIC bank was also allowed to acquire some of the deposits, assets, and liabilities of Imperial Bank as soon as the Kenya Deposit Insurance Corporation starts liquidating the bank (CBK, 2016). In 1995 several businesses came together and acquired a 60% stake in United Bank (Kenya). At that time, United Bank (Kenya) was under statutory administration by the Central Bank of Kenya since it was in receivership. In 1996, the bank rebranded to Chase bank and it opened its doors to customers once again. By December 2015, Chase Bank had an estimated value of KES 142 billion in asset valuation, At the same time, the shareholders' equity was valued at KES 11.9 billion (CBK, 2016). The Central Bank of Kenya placed Chase bank under receivership on April 7, 2016. The major causes for placement under receivership were associated with under-reporting of insider loans and failure to meet statutory banking ratios and therefore the bank was unable to meet its financial obligations and on April 2016 it was put under receivership by CBK. The insider loans stood at 13.62 billion Kenya shillings a figure way above the 5.72 billion Kenya shillings it reported. The bank made large amount of loan to its directors of about 13.62 billion Kenya shillings pointing to serious governance problem.

According to CBK report (2018), Kenyan Banking industry comprised 39 commercial banks, 13 microfinance banks, 1 mortgage finance company, 8 representative offices of foreign banks, 19 money remittance providers, 112 forex bureaus, 8 non-operating bank holding companies and 3 Credit Reference Bureaus in 2017. In 2017, Mayfair Bank Limited and DIB Bank Kenya Limited were licensed to operate banking business in Kenya. Central Bank of India (CBI) closed down its Representative Office while Société Générale of France opened a Representative Office in Kenya. In 2017, Giro Commercial Bank, Fidelity Commercial Bank Ltd and Habib Bank (K) Ltd were acquired by I & M Holdings Ltd, SBM Holdings Ltd, and Diamond Trust Bank Kenya Ltd respectively. (CBK, 2018)

The CBK report highlights that there was deterioration from 9.3 percent in December 2016 to 11.0 percent in December 2017 in asset quality, measured as a proportion of non-performing loans to gross loans, indicating an increase in credit risks in 2017. In actual amounts, there was a 23.4% growth in gross non-performing loans (NPLs) which moved from KSh.214.4 billion in December 2016 to KSh.264.6 billion in December 2017. Real estate, trade, manufacturing sectors and personal/household accounted for the largest share of Non-performing loans, at 73.1 percent of gross NPLs (CBK, 2018).

Comparison in terms of relationship between Non-Performing Loans and bank size, large tier group banks had lowest Gross NPLs to Gross Loans ratio which was below the industry average in 2017. Banks in the small and medium peer groups had 'Gross Non-performing loans to Gross Loans' ratios above the industry average in 2017. The report further points out that there was a decrease of 9.6 percent in the banking sector's pre-tax profits to Ksh.133.2 billion in December 2017 (CBK, 2018)

According to the report, total income in the industry decreased by 3.1 % in 2017 to Kshs. 486.3 billion, while total expenses fell by 0.5 % to Ksh.353.1 billion in December 2017. The decrease in profitability is attributed to high cost of deposits, reduce lending to the private sector, and slow economic growth in 2017 compared to 2016. Such declines in profitability undermine banks capacity to build capital buffers using retained earnings to absorb shocks. Return on Asset (ROA) and Return on Equity (ROE) of the banking sector have continued to decline since late 2016. ROA reached the lowest level of 2.3 percent in January 2017 while ROE touched the lowest level of 19.8 percent in February 2017. As at December 2017, ROE was 20.6 percent from 24.4 percent in December 2016 while ROA was 2.6 percent from 3.2 percent in December 2016. This Erosion of earnings over time may pose risks to financial stability through increased balance sheet risks. It also reduces build-up of capital buffers to absorb any shocks. Profitability was the most affected thing by the interest rates capping law which was introduced in 2015, although the decline started earlier in 2016 (CBK, 2018).

### *1.6. Statement of the Problem*

A number of theories have shown that, shareholders' objectives and corporate managers' objectives differ significantly and are contradictory as far as their individual interests are concerned and this has given rise to Corporate Governance where a Board of directors is constituted for the firm to be able to check and monitor the managers' actions and behavior. Corporate Governance challenges as confirmed by recent cases of bank failure witnessed in the banking sector in Kenya; collapse of Imperial Bank (2015), Dubai Bank (2015), and Chase Bank (2016) has sparked a lot of anger and uproar within the sector, these failures have been attributed to poor performance as a result of lack of adherence to sound Corporate Governance Practices leading to weak internal controls and weak management practices (CBK, 2016). Chase bank for example was placed under receivership because of under-reporting of insider loans especially advanced to the bank top management which had surpassed the ceiling leading the bank to fail to meet statutory banking ratios and therefore the bank was unable to meet its financial obligations, this was an indictment on the Board of Directors for failing on its responsibility in providing strategic leadership and ensuring sound Corporate Governance within the bank. This shows dealing with bank risks is still a challenge to the Boards of directors within the sector. Furthermore, bank failures are likely to have serious consequences to the country's economy and this will derail the achievement of Kenya vision 2030.

Recent report released by the Central Bank of Kenya (CBK, 2018) on the general industry performance points a picture of performance challenges within the sector since most performance parameters have been declining in the recent past, according to the report, there was a decrease of 9.6 percent in the banking sector's pre-tax profits from 147.3 billion to Ksh.133.2 billion in December 2017, Such declines in profitability undermine banks capacity to build capital buffers using retained earnings to absorb shocks.

In a bid to find out the connection between corporate governance and firm performance, several studies have been undertaken. Olick (2015) concluded in a research study that the board size (in terms of membership number) has a positive and significant impact on the Return on Asset ratio (ROA). Batool and Gohar (2015) found that large boards of directors inversely influence the financial performance of firms but also has a positive effect on corporate social responsibility and reputation.

Carty and Weiss (2012) found no correlation between bank failure and CEO duality while the study results by Al-shammari and Al-saidi (2013) indicates that CEO duality positively impacts the performance of banks. Zhaoyang and Udaya (2012) concluded that firms' size of the Board and non-executive directors' composition in the whole board structure revealed a negative correlation to the value of the firm, also the effect of non-executive directorship on the financial performance of the firm was negative. In the local context, Adhiambo (2014) concentrated on board size and found that a large board size tend to impact performance negatively, Kalungu (2012) study on the impact of corporate governance on financial performance of commercial banks in Kenya narrowed down on a few variables of corporate governance practices, it concentrated on three board elements: Board size; board composition and board monitoring. In the Kenyan context, the available studies reveal some trend of inconclusiveness since they tend to study this relationship using two variables at a time; dependent and independent variables while ignoring other factors or interactions that may be important within the governance and performance framework of these institutions. However, to bridge this gap, this study considered the relationship between executive compensation and the performance of commercial banks in Kenya while incorporating strategic leadership as a moderating variable to this relationship. This study utilized correlation design and a census on all the thirty-nine operating commercial banks in Kenya where data was purposively collected from all the CEOs and one executive Director from each bank later analysed using Ordinal Logistic Regression Analysis to establish the relationship among the study variables.

### 1.7. Study Objectives

The main objective of this study was to examine the moderating effect of strategic leadership on the relationship between executive compensation and firm performance. Specifically, this study sought to address the following objectives:

- To establish the influence of Share ownership by top management on the performance of commercial banks in Kenya.
- To determine the influence of payment of executive perks on the performance of commercial banks in Kenya
- To determine the relationship between bonus payment and performance of commercial banks in Kenya
- To examine the moderating effect of strategic leadership on the relationship between executive compensation and the performance of commercial banks in Kenya.

### 1.8. Research Hypotheses

In order to generate useful answers to realize the objectives of the study, the following null hypotheses were tested:

- There is no significant relationship between Share ownership and performance of commercial banks in Kenya.
- There is no significant relationship between Executive perks and performance of commercial banks in Kenya
- There is no significant relationship between Bonus payment and performance of commercial banks in Kenya
- Strategic leadership has no significant moderating effect on the relationship between executive Compensation and performance of commercial banks in Kenya.

## 2. Literature Review

### 2.1. Theoretical Literature Review

#### 2.1.1. Contingency Theory

This is a leadership theory that was postulated by House (1996) where he indicated that the contingency approach to management is premised on the idea that there is no specific way of managing an organization by planning, organizing, staffing, controlling and leading, instead the approach of management employed must be tailored to suit the specific circumstances facing the organization. Lutans (2011) asserts that a strategic leader's effectiveness is highly depended on how he navigates and manages the demands imposed by specific situations.

The contingency theory states that rather than using a "one size fits all" method to handle situations leaders make managerial decisions depending on the situation at hand. According to this theory the best leadership style is flexible and dynamic. A participative leadership approach should be adopted by a leader where they should involve their employees in key decisions concerning performance management by clearly explaining to them how important their performance is, its impact on them and how it impacts the organization as a whole (Lutans, 2011).

Kjelin (2009) defines Strategic leadership as the ability of firms to envision, anticipate and maintain flexibility, and empower others to create a strategic opportunity and a reliable future of the organization. Strategic leadership as defined by Guillot (2003) is the ability of, a senior leader who is experienced and has wisdom and vision to make and execute plans and make consequential decisions in the uncertain, volatile, complex and ambiguous strategic business environment.

Pearce and Robinson (2007) assert that coping with change is the hallmark of strategic leadership; and more leadership is always demanded when more change is needed. According to Hitt, Ireland, and Hoskisson (2007) strategic leadership is the ability on the part of the leader to envision, anticipate and maintain organizational flexibility, by empowering others in order for the necessary strategic changes to be created; it entails managing through others. Strategic leadership according Capon (2008) is the ability to positively influence a group of people towards achieving goals. He affirms that good leadership carries strategic vision that is clear and persuasive at implementing the stated strategy to achieve tangible results for the organization. Lynch (2009) views strategic leadership as one which involves communicating with and listening to those within the organization with a great aim of creating and spreading knowledge, creation and innovation of new ideas in specific areas and provision of solutions to problems. Lynch (2009) clarifies that Strategic leadership involves a multifaceted balancing act among a number of factors. It entails dealing with variations and pressures from the environment outside the organization while at the same time dealing and managing the critical human resources within the organization. Strategic leadership according to Rowe et al. (2001) is the ability of the leader to drive other people to voluntarily make conscious decisions that enhance the institution viability while still maintaining the financial stability of the organization in the short-term. He further points out that to be effective; a strategic leader must be in a position to visualize their ideas into images that create excitement among people as they work. According to Hitt et al. (2007) efficient and effective strategic leadership obligation rests at the top of the organization, specifically with the firm's chief executive officer (CEO). However, the other generally known strategic leaders within the organization are the board of directors (BOD), divisional general managers, and of course the entire top management team. These leaders have extensive decision-making tasks that cannot be delegated.

According to Kumar et al. (2002), the concept of *Client centrlicity* entails strategic leadership attributes that stimulates an organizational culture that places the customer at the center of the organization's business while focusing and thinking about strategy and operations as well. Hence, this concept puts focus on the environment and deals with the exploitation of current client accounts. Colgate and Danaher (2000) state that in a highly competitive business environment, one of the most crucial business tenets is customer retention, without senior leadership support, a customer orientation is unlikely to take root in an organization. Liao and Subramony (2008) stated that oriented values and beliefs

are uniquely the responsibility of top management, only the Chief Executive Officer can take responsibility for defining customer values that are harmonious with customer satisfaction to the organization stakeholders. The organizational behavior must be consistent with customer-oriented mandates (Liao & Subramony 2008). The resulting strategic leadership model is composed of four quadrants, i.e. Organizational creativity, Business development, Client centricity and Operational efficiency along the two dimensions Exploration-Exploitation and Organization-Environment (Hester, 2013). Contingency theory, although having several strengths, generally falls short in trying to explain why leaders with certain leadership styles are effective in some situations but not in others. Contingency theory also fails to adequately explain what should be done about a leader/situation mismatch in the workplace (Northouse, 2007).

### 2.1.2. Stewardship Theory

Donaldson and Davis (1991) proposed this theory and holds that there is no inherent, general problem of executive motivation. "The executive manager, under this theory, far from being an opportunistic shirker, essentially wants to do a good job, to be a good steward of the corporate assets." According to stewardship theory, performance variations arise, not from inner motivational problems among executives, but from whether the structural situation in which the executive is located facilitates effective action by the executive.

This theory posits that managers are seen as good stewards who will always take organizational decisions in the best interest of the shareholders (Donaldson & Davis, 1991). Social psychology, which mainly majors on the executives' behaviour, is the fundamentals of stewardship theory. The stewards' behaviour is collectivists and pro-organizational, and the behavior of the steward will not depart from the interest of the firm since the steward always seeks to attain the objectives of the firm (Eddleston and Kellermanns (2007).

Smallman (2004) is of the opinion that, there is maximization of the steward's utilities where there is maximization of shareholder's wealth, because most requirements will be served by organizational success and hence the stewards will have a clear mission. He also states that, the steward will balance tensions between different beneficiaries and other interest groups in a firm. Therefore, stewardship theory is an argument put forward in the performance of the firm that satisfies the interested parties' requirements leading to dynamic performance equilibrium for balanced governance. According to Stewardship theory managers protect and maximize shareholder wealth through firm performance and therefore, the theory sees a strong relationship between success of the firm and the managers. Corbetta and Salvato (2004) asserts that Successful performance improvement by a steward satisfies most stakeholder groups in an organization, when these groups have interests that are well served by increasing organizational wealth. The power to determine strategy and the fate of the organization is the responsibility of a single person when the position of the chairman and the CEO is held by a single person in an organization, thus rather than control and monitor the focus of stewardship theory is on structures that empower and facilitate (Corbetta & Salvato, 2004). Therefore, stewardship theory does not see the need to separate the position of the CEO and chairman, and it supports the appointment of a single person for the role of CEO and chairman and a majority of specialist executive directors rather than non-executive directors (Clarke, 2004). According to Zahra et al. (2009) Stewardship theory focuses on a two-party contract of employment relationship; the owner of the business who is the principal and the steward who is the manager. It also looks at this relationship from a behavioral perspective and structural perspective. Zahra et al., (2009) states that the proposal by this theory is that because managers are stewards, they will act in a manner that is pro-social, actions which are aligned with the principal's interests and thus the organization. Corbetta and Salvato (2004) continues to affirm that this steward's behavior is reinforced by three things; quality of the relationship between the steward, principal and the organizational environment. A stewardship perspective is about maximum organizational performance, which is reflected in sales growth and profitability as they are the desired outcome of any performance (Davis et al., 1997; Tosi et al., 2003).

This outcome according to Eddleston and Kellermanns (2007) is achieved when both the principal and the manager in the employment relationship decide to behave and make decisions that reflect the element of stewardship. The heart of this theory is the assumption that the steward- principal relationship is based on a choice. Eddleston and Kellermanns (2007) asserts that When both parties choose to behave like stewards by placing the interest of the principal first, then, there is a positive effect on performance because the two parties are working on a common goal Corbetta and Salvato (2004) and Vallejo (2009) indicates that the choice of stewardship behavior is as a result of both situational factors and psychological factors such as intrinsic motivation, high identification, and personal power can steer the behavioral choice to stewardship. Intrinsic motivation provides satisfaction in and of itself since it exists within individuals (Ryan & Deci, 2000). Intrinsic motivation is a psychological attribute of stewardship theory because managers who are stewards are motivated by intangible, higher order rewards (Davis et al., 1997; Lee & O'Neill, 2003). The suggestion by the theory is that involvement-oriented, low power distance collectivist and cultures help influence the stewardship choice of behaviour (Vallejo, 2009). An involvement-oriented management philosophy is portrayed by an environment where employees are trusted with opportunities, responsibility and challenges (Eddleston et al., 2012; Vallejo, 2009). Individuals give priority to the goals of the collective rather than individual personal goals in organizations typified by collectivism; the emphasis is on capturing, belonging and displaying loyalty due to the tight-knit organizational social framework present in the firm (Davis et al., 1997; Nicholson, 2008). Stewardship theory suggests that to have a greater role of stewardship in the organization and good management then the role of the CEO and the chairman should be unified so as to minimize agency costs. It is evident that there would be better safeguarding of the interest of the shareholders (Vallejo, 2009).

The motivation of the CEOs and facilitative empowering structures that fusion the incumbency roles of the organization's CEO and chairman that enhance effectiveness leading to superior firm performance is the focus of Stewardship theory. According to the Stewardship theorists smaller board sizes promote increased participation and

social cohesion unlike a larger board size which often hinders the board's ability to reach agreements on important decisions (Vallejo, 2009). They further argue that: executive dominated boards should be favored by organizations because of their ability to access current information on organizational operations, their depth of knowledge, technical expertise, and commitment to the company that potentially impact on organizational performance positively (Letting" *et al.* 2012). According to the Central Bank of Kenya, banks should embrace a board of whom 1/3 should be women and 3/5 of the members should be independent directors drawn from various professions and as a source of various professional opinions and to cater for gender parity that may be required for smooth running and enhanced performance of banks (CBK, 2013).

A drawback with stewardship theory is seen to be the fact that a greater transaction cost outlay will be made as there will be more investment of time for the principal in involving the steward in resolving problems, joint decision-making and information exchange (Van, 2006). The theory is sometimes criticized on the basis that it gives directors *carte blanche* when it comes to exercising their discretion, but it must be acknowledged that boards are constrained by a number of factors such as the availability of an appropriate workforce, the demand for the products of the company and the cost and availability of finance (Blair & Stout 2001).

## 2.2. Empirical Literature Review

A study carried out by Sigler (2013) examined the relationship between CEO pay and firm performance for a period from 2006 through to 2009 on 280 firms which are listed on the New York Stock Exchange. The time frame of this study was a period after the adoption of the Sarbanes Oxley Act of the corporate governance rules affecting executive pay for companies listed in the New York Stock Exchange. The study adopted both descriptive and inferential statistics, and the findings indicated a positive and significant relationship between CEO compensation and organization performance measured by return on equity. The size of the company was also discovered to be the most significant factor in determining the level of CEO compensation. The tenure of the CEO is another significant variable that influences return on equity according to the results of this study. In this study, the CEO pay was proxy by, cash compensation monthly, salary and total compensation. A study by Mehul and Surenderrao (2016) examined the relationship between executive compensation and firm performance among Indian firms. The evidence suggests that executive compensation significantly affects firm performance measured by accounting, as well as market-based measures. Sanders and Boivie (2004) investigated the case of corporations designated as Internet Firms of the United States and they concluded that the market valuation of those corporations was strongly related with the level of compensation incentives based on stocks.

Nuray and Moazzam (2016) conducted a study in Bangladesh to investigate the effect of compensation on job performance. Various items of compensation and Job Performance items were taken into consideration for measuring their effect. The study used a questionnaire to collect data from 261 respondents who were working in twenty different readymade garment organizations. The quantitative analysis results indicated that there is a strong and positive relationship between compensation and job performance.

A study conducted by Chen, Fan, and Shen (2015) on the relationship between employees and executives' compensation on organizational performance among the firms in China revealed that compensation of executives and employees are both positively associated with the performance of enterprises, which indicates the two kinds of compensation incentive have a positive effect on the growth of enterprise performance. The study also revealed that the pay-performance sensitivity of executives is significantly higher than that of employees. Moreover, the stronger the synchronization between the compensation of employees and that of executive is, the bigger the encouraging effect on future performance is. Steven *et al.* (2011) investigated the relationship between the use of performance measures in executive compensation and firm strategy. Their study analysis showed that there is an increased emphasis on sales in the determination of executive compensation for firms pursuing a cost leadership strategy in order to attain competitive advantage through low price and high volume while there is a decreased emphasis on accounting measures in firms pursuing a differentiation strategy, which require investments in brand recognition and innovative products, investments that are subject to unfavorable accounting treatment. These results indicate that executive rewards are linked to firm strategy by compensation committees. Obasan (2012) conducted a study on the effect of Compensation Strategy on Corporate Performance among the Nigerian Firms. Using the cross-sectional data analysis, the study found that compensation strategy has the potential beneficial effects of enhancing workers' productivity and by extension improving the overall organizational performance. Therefore, the study concluded that the significance of compensation cannot be overemphasized in an organization and is in fact a veritable option for attracting, retaining, and motivating employees for improved organizational productivity. The findings of this study further enriched the literature supporting that a higher pay guarantees a higher productivity and vice-versa.

## 3. Research Methodology

This study employed correlational research design. This type of design is basically concerned with evaluating the relationships between and among study variables. It is anchored on the ground that using the information available on the independent variables, it is possible to predict the dependent variable and whether a relationship exists between the two variables that is statistically significant.

Kothari (2004) asserts that a correlational research design is utilized to explore the effect of one variable on another and this is consistent with this study which sought to establish the relationship between Board composition and bank performance. The basic empirical investigation here was to determine whether there exists a relationship between board composition variables and performance of commercial banks.

The target population for this study was all the Thirty-nine (39) operating commercial banks in Kenya; a survey was conducted on the 39 commercial banks that are licensed and operating in Kenya. The study used purposive sampling where thirty nine (39) Chief Executive Officers (CEOs), one from each bank in whose absence one of the executive directors was used as the respondents and thirty nine (39) executive directors, one from each bank were also involved in giving responses to the questionnaires thereby giving a sample size of seventy eight (78). This is because Chief Executive Officers of the respective banks are better placed to give accurate answers concerning the performance of their banks and executive directors are in a better position to provide independent answers on compensation. Primary data was collected from the respondents using questionnaires which were structured into two main parts ; part I and part II, where part I generated data that provided background information about the respondent, while part II was arranged systematically according to the study objectives to generate data that gave information that was used to test the research hypotheses. The questionnaires comprised of both open-ended and Likert scale questions.

### 3.1. Data Analysis

The response variable in this study was the increase in profitability of the bank which was categorised into three hierarchical levels - large, moderate and less. The research therefore used the Generalised Linear Model (GLM) in the form of ordinal logistic regression as the main technique in the analysis of data using R Technique.

### 3.2. Ordinal Logistic Regression Technique

Bank performance was taken as the response variable and denoted by  $Y$ . Each  $Y_i$  has three levels measured on a three-point Likert scale as large, moderate and less. Based on the ranks, the three levels of  $Y$  can be arranged in a hierarchical manner as:

$Large > moderate > less$

Based on the measurement scale of the response variable  $Y_i$  the research used the ordinal logistic regression technique. Assuming a proportional odds model, with the level less taken as the reference category, two ordinal logistic regression models were fitted simultaneously on to the data.

$$\left[ \frac{P(Y = less)}{P(Y = moderate, large)} \right] = \exp(\beta_{01} + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \dots + \beta_k X_k)$$

$$\left[ \frac{P(Y = less, moderate)}{P(Y = large)} \right] = \exp(\beta_{02} + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \dots + \beta_k X_k)$$

For the categorical explanatory variables, this technique outputs a measure called the odds ratio, which gives a relative measure of the probability of one categorical value(s) occurring against the probability of another categorical value(s) not occurring. The ordinal logistic regression with proportional odds uses cumulative categories, and therefore the intercept differs between the pair of models, but the regression co-efficients are the same across the two fitted models. Therefore, given a categorical explanatory variable  $X_i$  and the regression co-efficient  $\beta_i$ , the odds ratio denoted by OR is given by:

$$OR = \exp(\hat{\beta}_i)$$

### 3.3. Assumptions in the Ordinal Logistic Regression Model

- Linearity: There is a linear relationship between each explanatory variable  $X_i$  and the logarithm of the response variable  $Y$ .
- Independence of errors: Data for observational units are not related. Same data is not collected from same respondents at different times.
- No perfect multi-collinearity: The observations are independent and therefore no relationship exists between multiple explanatory variables. This means the explanatory variables are independent of each other.

### 3.4. Interpretation and Inference

#### 3.4.1. Interpretation of the Regression Co-efficient and Odds Ratio

The odds ratio can be less than 1, equal to 1 or greater than 1. A value of 1 means 100%.

If the odds ratio is greater than 1;  $\beta_i > 0 \Leftrightarrow \exp(\hat{\beta}_i) > 1$

Then it means that the other category of interest is (OR% - 100%) more likely to have the characteristic of interest in  $X_i$  than the reference category.

If the odds ratio is less than 1 ;  $\beta_i < 0 \Leftrightarrow \exp(\hat{\beta}_i) < 1$

Then it means that the other category of interest is (100% - OR %) less likely to have the characteristic of interest in  $X_i$  than the reference category.

If the odds ratio is equal to 1 ;  $\beta_i = 0 \Leftrightarrow \exp(\hat{\beta}_i) = 1$

Then it means that the other category of interest and the reference category are equally likely and therefore the characteristic of interest in  $X_i$  does not influence the response variable.

Also, generally, the more the odds ratio deviates from 1 (the more the co-efficient deviates from 0), the stronger the relationship between the values of  $X_i$  and  $Y_i$ .

3.4.2. Inference on the Regression Co-efficient

To test for the significance of the co-efficient  $\beta_i$ , the research formulated the hypothesis:

$H_0: \beta_i = 0,$

$H_1: \beta_i \neq 0,$

The 95% confidence limits for the co-efficient  $\beta_i$  is given by

$\beta_i = \hat{\beta}_i \pm t_{\alpha/2} S_{\hat{\beta}_i} \Leftrightarrow \beta_i = \hat{\beta}_i \pm t_{0.25} S_{\hat{\beta}_i}$

Where  $z$  is the Wald's test statistic given by:

$$t = \frac{\hat{\beta}_i - \beta_i}{S_{\hat{\beta}_i}}$$

If the confidence interval for the co-efficient  $\beta_i$  includes the value 0, then the research fails to reject the null hypothesis  $H_0: \beta_i = 0$ , and it is therefore concluded that the corresponding explanatory variable  $X_i$  does not make a statistically significant contribution to the response variable  $Y$ , otherwise if the confidence interval for the co-efficient excludes the value 0, then the null hypothesis  $H_0: \beta_i = 0$  is rejected, and it is therefore concluded that the variable  $X_i$  makes a significant contribution in determining the response variable  $Y$ .

4. Research Results and Discussion of Findings

4.1. Correlation Analysis

The problem of multi-collinearity was solved by computing the correlation matrix for each set of independent variables in the same group in terms of all objectives. Further the technique of principal component analysis was used to identify and cluster a group of related variables which have a high correlation and therefore assumed to measure the same traits. Within a cluster the strongest variable which has the highest value (loading) in the rotated component matrix was selected to represent the cluster.

4.2. Compensation System

The inter-item correlation matrix in table 4.6 shows the correlation among the executive compensation system variables; putting in place a Compensation scheme for the top management, having other Perks for executive apart from monthly salaries, performance based bonus payment and allowing top management share ownership of the organization; the matrix shows a positive correlation for all the items meaning they all measure in the same direction the underlying characteristics.

	Compensation Scheme - mng	Perks for Executive	Bonus Payment	Share Ownership by Executive
Compensation scheme - mng	1.000	0.084	0.081	0.053
Perks for Executive	0.084	1.000	0.193	0.493
Bonus payment	0.081	0.193	1.000	0.109
Share ownership by executive	0.053	0.493	0.109	1.000

Table 4.1: Executive Compensation System Correlation Matrix

The technique of principal component analysis was used to identify and cluster a group of related variables which have a high correlation and therefore assumed to measure the same traits within the Compensation variable. Within a cluster the strongest variable which has the highest value (loading) in the rotated component matrix was selected to represent the cluster. Table 4.7 shows allowing share ownership of the company by top management and putting in place a compensation scheme for the top management had the highest loading factor and therefore were picked to represent the cluster of Compensation system.

	Component	
	1	2
Share ownership by executive	0.851	0.021
Compe scheme	0.843	0.150
Executive perks for top mng	-0.089	0.877
Bonus payment	0.262	0.544

Extraction Method: Principal Component Analysis.  
Rotation Method: Varimax with Kaiser Normalization.<sup>a</sup>

Table 4.2: compensation system Rotated Component Matrix<sup>a</sup>  
a. Rotation converged in 3 iterations

The reduced model therefore becomes

$$\left[ \frac{P(Y = less)}{P(Y = moderate, large)} \right] = exp(\beta_{01} + \beta_1 X_1 + \beta_2 X_2)$$

$$\left[ \frac{P(Y = less, moderate)}{P(Y = large)} \right] = exp(\beta_{02} + \beta_1 X_1 + \beta_2 X_2)$$

- $X_1$  - Share ownership by executive  
 $X_2$  - Payment of executive perks

#### 4.3. Regression Analysis

Models were derived for the objectives based on the reduced number of variables. Because the explanatory variables are categorical, except for the reference category, each other category was assigned a regression co-efficient  $\beta_i$  and interpreted separately.

#### 4.4. Executive Compensation System and Performance of Commercial Banks

Table 4.3 shows the coefficients resulting from the regression analysis among the representing variables of compensation system, the moderating variable (offering of strategic direction by the board) and bank performance (profitability)

Regression analysis was used to test the research hypotheses, determine the existence of a significant relationship between the variables under the study and to ascertain the predictive power of executive Compensation system variables on bank performance and also ascertain the same power when strategic leadership is introduced into the relationship.

Coefficients:	Estimate			Odds Ratio	
	Value	Std. Error	t-value	$exp(\hat{\beta}_i)$	
	$\beta_i$			Absolute	Percentage
Model 1: 2 3	5.89	1.84	0.67	3.633	363.3%
Model 2: 3 4	-2.49	1.26	0.81	0.082	8.2%
Exec perks4	-3.36	2.13	1.80	0.035	3.5%
Exec perks5	-1.10	1.49	-0.74	0.333	33.3%
ShareOwn3	-0.30	5.01	-0.01	0.742	74.2%
ShareOwn4	-9.02	4.87	1.29	0.0001	0.0%
ShareOwn5	-8.17	3.76	0.82	0.0003	0.0%
StratDirect3	2.14	3.09	0.20	8.499	849.9%
StratDirect4	2.48	0.69	2.40	1.197	119.7%
StratDirect5	3.50	1.28	1.64	3.308	330.8%
Exec perks4:StratDirect4	3.87	0.69	2.40	4.770	477.0%
Exec perks4:StratDirect5	3.58	3.86	1.47	3.602	360.2%
ShareOwn3:StratDirect3	3.47	7.81	-0.19	3.214	321.4%
ShareOwn3:StratDirect4	4.16	5.57	0.37	6.407	640.7%
ShareOwn4:StratDirect4	5.28	4.60	1.60	1.972	197.2%

Table 4.1: Compensation System Regression Analysis

The two ordinal logistic regression models for board composition factors are therefore fitted onto the data.

$$\left[ \frac{P(Y = \text{less})}{P(Y = \text{moderate}, \text{large})} \right] = \exp(5.89 - 3.36X_1 - 1.10X_2 - 0.30X_3 - 9.02X_4 - 8.17X_5 + 2.14X_6 + 2.48X_7 + 3.50X_8 + 3.87X_9 + 3.58X_{10} + 3.47X_{11} + 4.16X_{12} + 5.28X_{13})$$

$$\left[ \frac{P(Y = \text{less}, \text{moderate})}{P(Y = \text{large})} \right] = \exp(-2.49 - 3.36X_1 - 1.10X_2 - 0.30X_3 - 9.02X_4 - 8.17X_5 + 2.14X_6 + 2.48X_7 + 3.50X_8 + 3.87X_9 + 3.58X_{10} + 3.47X_{11} + 4.16X_{12} + 5.28X_{13})$$

Compensation scheme: large  $\beta_i = -3.36$ , therefore  $exp(\hat{\beta}_i) = 0.035$

Therefore, a bank which to a large extent has put in place a compensation scheme for top management is 96.53% less likely to increase profits compared to a bank which to less extent has put in place a compensation scheme for top management. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [-7.196, 0.472] which includes 0.

Compensation scheme: very large  $\beta_i = -1.10$ , therefore  $exp(\hat{\beta}_i) = 0.333$

Therefore, a bank which to a very large extent has put in place a compensation scheme for top management is 66.75% less likely to increase profits compared to a bank which to a less extent has put in place a compensation scheme for its top management. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [-0.019, -2.202] which excludes 0.

Share ownership: moderate  $\beta_i = -0.30$ , therefore  $exp(\hat{\beta}_i) = 0.742$

Therefore, a bank which to a moderate extent has allowed members of the executive share ownership is 25.84% less likely to increase profits compared to a bank which to less extent has allowed members of the executive share ownership. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [-0.27, -0.33] which excludes 0.

Share ownership: large  $\beta_i = -9.02$ , therefore  $\exp(\hat{\beta}_i) = 0.0001$

Therefore, a bank which to a large extent has allowed members of the executive share ownership is 99.9% less likely to increase profits compared to a bank which to less extent has allowed members of the executive share ownership. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [-15.30, -2.73] which excludes 0.

Share ownership: very large  $\beta_i = -8.17$ , therefore  $\exp(\hat{\beta}_i) = 0.0003$

Therefore, a bank which to a very large extent has allowed members of the executive share ownership is 25.84% less likely to increase profits compared to a bank which to less extent has allowed members of the executive share ownership. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [-11.25, -5.09] which excludes 0.

Compensation scheme: large and strategic direction: large

$\beta_i = 3.87$ , therefore  $\exp(\hat{\beta}_i) = 4.77$

Therefore a bank whose board has put in place a compensation scheme for top management to a large extent and offers strategic direction to a large extent is 4.8 times more likely to increase profits from one level to the next compared to a bank whose board has put in place compensation scheme to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [2.21, 5.52] which excludes 0.

Compensation scheme: large and strategic direction: very large

$\beta_i = 3.58$ , therefore  $\exp(\hat{\beta}_i) = 3.602$

Therefore a bank whose board has put in place a compensation scheme for top management to a large extent and offers strategic direction to a very large extent is 3.6 times more likely to increase profits from one level to the next compared to a bank whose board has put in place compensation scheme for top management to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [-2.078, 9.246] which includes 0.

Share ownership: moderate and strategic direction: moderate

$\beta_i = 3.47$ , therefore  $\exp(\hat{\beta}_i) = 3.214$

Therefore a bank whose board has allowed members of the executive share ownership to a moderate extent and offers strategic direction to a moderate extent is 3.2 times more likely to increase profits from one level to the next compared to a bank whose board has allowed members of the executive share ownership to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [4.945, 9.949] which excludes 0.

Share ownership: moderate and strategic direction: large

$\beta_i = 4.16$ , therefore  $\exp(\hat{\beta}_i) = 6.407$

Therefore a bank whose board has allowed members of the executive share ownership to a moderate extent and offers strategic direction to a large extent is 6.4 times more likely to increase profits from one level to the next compared to a bank whose board has allowed members of the executive share ownership to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [2.088, 6.232] which excludes 0.

Share ownership: large and strategic direction: large

$\beta_i = 5.28$ , therefore  $\exp(\hat{\beta}_i) = 1.972$

Therefore a bank whose board has allowed members of the executive share ownership to a large extent and offers strategic direction to a large extent is 2 times more likely to increase profits from one level to the next compared to a bank whose board has allowed members of the executive share ownership to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives interval [2.067, 12.634] which excludes 0.

- Hypothesis 1: There is no significant relationship between Share ownership and performance of commercial banks in Kenya

The results from regression analysis (Table 4.3) indicate that a bank which to a large extent has allowed members of the executive share ownership of the company is 25.84% less likely to increase profits compared to a bank which to less extent has allowed members of the executive share ownership. Testing of the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives [-15.30, -2.73] which excludes 0 value. Therefore, the research rejects the null hypothesis at the 5% level of significance and concludes that allowing share ownership of the company by the bank top management is a statistically significant factor that influences commercial banks' performance in Kenya. Introducing strategic direction into the relationship as a moderating variable indicates that a bank which has allowed members of the executive share ownership to a large extent while offering strategic direction to a large extent is 2 times more likely to increase profits from one level to the next compared to a bank whose board has allowed members of the executive share ownership to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives [2.067, 12.634] which excludes 0. Therefore, the research rejects the null hypothesis at the 5% level of significance and concludes that allowing share ownership to top management while offering strategic direction by the board is a statistically significant factor that influences the performance of commercial banks in Kenya.

- Hypothesis 2: There is no significant relationship between payment of executive perks and performance of commercial banks in Kenya

The results from the regression analysis (Table 4.3) indicate that a bank which to a very large extent pays executive perks to top management is 66.75% less likely to increase profits compared to a bank which to less extent pays

executive perks to top management. Testing the null hypothesis at 95% confidence interval gives  $\beta_i$  co-efficient interval [-0.019, -2.201] which excludes 0 value.

Therefore, the research rejects the null hypothesis at the 5% level of significance and concludes that paying competitive executive perks to top management is a statistically significant factor that influences performance of commercial banks in Kenya. These findings are in line with the study by Mehul and Surenderrao (2016) which examined the relationship between executive compensation and firm performance among Indian firms, based on the empirical findings the study concluded that executive compensation is a factor that significantly affects firm performance.

Introducing strategic direction into the relationship as a moderating variable indicates that a bank which pays executive perks to top management to a large extent and offers strategic direction to a large extent is 4.8 times more likely to increase profits from one level to the next compared to a bank which pays executive perks to a less extent and offers strategic direction to a less extent. Testing the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives [2.21, 5.52] which excludes 0 value. Therefore, the research rejects the null hypothesis at the 5% level of significance and concludes that paying executive perks to top management while offering strategic direction by the board is a statistically significant factor that influences the performance of commercial banks in Kenya. According to Stewardship theory managers protect and maximize shareholder wealth through firm performance and therefore, the theory sees a strong relationship between success of the firm and the managers. Corbetta and Salvato (2004) asserts that Successful performance improvement by a steward satisfies most stakeholder groups in an organization, when these groups have interests that are well served by increasing organizational wealth.

The power to determine strategy and the fate of the organization is the responsibility of a single person when the position of the chairman and the CEO is held by a single person in an organization, thus rather than control and monitor the focus of stewardship theory is on structures that empower and facilitate the workings of the managers including giving them good compensation (Corbetta & Salvato, 2004).

Given that the relationship between payment of executive perks and performance of commercial banks in Kenya is significant, we therefore reject the null hypothesis that there is no significant relationship between executive perks and the performance of commercial banks in Kenya and fail to reject the alternative hypothesis that there is a significant relationship between payment of competitive executive perks and performance of commercial banks in Kenya and therefore conclude that putting in place a system of paying executive perksto the top bank management is a factor that influences performance of commercial banks in Kenya.

- Hypothesis 3: Strategic leadership has no significant moderating effect on the relationship between executive compensation system and performance of commercial banks in Kenya.

Strategic leadership measured by giving of strategic direction by the board was used as a moderating or interaction variable in the relationship between the various independent variables and performance of commercial banks which was the response variable. When combining payment of executive perks and offering strategic leadership by the Board of Directors, table 4.3 indicate that a bank which pays competitive executive perks to top management to a large extent and offers strategic direction to a large extent is 4.8 times more likely to increase profits from one level to the next compared to a bank which pays executive perks to a less extent and has put in place strategic direction to a less extent. Testing of the null hypothesis at 95% confidence interval for co-efficient  $\beta_i$  gives [2.21, 5.52] which excludes 0 value. Therefore, the research rejects the null hypothesis at the 5% level of significance and concludes that paying executive perksto the top management of the bank and offering strategic direction by the board is a factor that is statistically significant in influencing the performance of commercial banks in Kenya.

Generally, combining strategic leadership with the independent variables leads to the rejection of null hypotheses. We therefore conclude that strategic leadership moderates the relationship between executive Compensation system and the performance of commercial banks in Kenya and reject the null hypothesis that Strategic leadership has no significant moderating effect on the relationship between executive compensation system and performance of commercial banks in Kenya. The findings above validate a study by Bader (2016) which examined the effect of both innovation and strategic orientation on organizational performance. It also examined the mediation effect of innovation on strategic orientation and organizational performance. Data were collected from the three telecommunication companies in Jordan. The data analysis was done using Structural Equation Modeling (SEM) and the results showed a significant effect of strategic orientation on innovation and organizational performance. It was also discovered that innovation significantly affected firm performance. Finally, the results showed that innovation partially mediated the path between strategic orientation and organizational performance.

## 5. Conclusions

The main objective of this study was to examine the moderating effect of strategic leadership on the relationship between executive compensation system and firm performance. Given the empirical findings, this study therefore concludes that offering strategic leadership by the board of directors is a significant factor that moderates the relationship between executive compensation system and the performance of commercial banks in Kenya.

The study concludes that allowing share ownership of the organization by top management is a statistically significant factor that influences the performance of commercial banks in Kenya. The study alsoconcludes that there is a significant relationship between payment of executive perks to top management and the performance of commercial banks in Kenya. The study further concludes that offering strategic leadership by the Board of Directors is a statistically significant factor that moderates the relationship between executive compensation system and the performance of commercial banks in Kenya. Strategic leadership variables like offering organizational direction by clearly setting and disseminating the organizational vision, mission and strategic objectives to the bank employees, managing change in the ever changing

business environment, putting customers' interests in the center of bank operations are all critical factors that significantly moderate the relationship between executive compensation system and the performance of commercial banks in Kenya.

## 6. Recommendations

In view of the findings that strategic leadership moderates the relationship between executive compensation system for top management and performance of commercial banks in Kenya, Board of Directors should establish a system that allows top executive share ownership of these banks, this will induce the top management to align their interests to the interest of these banks and subsequently work to improve the performance of these banks. Banks should establish a system that competitively pays top management perks other than monthly salaries as a way of motivating them to enhance organizational performance. Since the findings of this study reveal that there is significant moderating effect by strategic leadership on relationship between executive compensation system and the performance of commercial banks in Kenya, Boards of Directors should offer strategic management leadership, they should draw strategic plans detailing clear strategic objectives on key areas of operation like finance, human resource, credit and customer. The same should clearly be disseminated to all bank employees with the view to having them buy in and direct their efforts to productive areas. Banks should also employ people with strategic orientation especially at the top-level management and invest resources in developing strategic leadership in order to enhance their performance

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