

**EFFECT OF EMPLOYEE SHARE OWNERSHIP PLANS ON
FINANCIAL PERFORMANCE
OF FIRMS LISTED IN THE NAIROBI SECURITIES EXCHANGE**

BY

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DECLARATION

I, Augustine Khisa, do hereby declare that this research project is my original work and has not been, and is not currently being submitted for a degree in any other university.

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Date

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This research project has been submitted for examination with my approval as the University supervisor.

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I thank my immediate family members for their love, support and encouragement to always reach the pinnacle of education.

DEDICATION

To my immediate family members for their patience and unfailing moral support throughout my period of study and for understanding and appreciating the demand of the course in terms of time and resources, to my Supervisor for guidance and to God for his providence.

ABSTRACT

Employee share ownership is commonly recognized as an adequate method for spurring firm performance by facilitating employees to participate in the creation and sharing of wealth they create in an organization. The reason is that Employee Stock Ownership Plans (ESOPs) realign employee's goals with corporate goals and help companies to attract talent, retain staff, motivate employees and enable them to share the long-term growth of the company. Previous empirical studies provide contradictory conclusion with some positing that ESOPs enhance company performance and others arguing that just like stock options, ESOPs had a net unfavorable effect on performance of a company in the long run.

The study investigates the effect of ownership of shares by employees on financial performance of listed firms in the NSE. This study was conducted through the use of a descriptive design. Population of study comprised of all companies listed in the NSE operating in Kenya during the study period. The study used purposeful sampling to pick 8 companies listed in the NSE having employee stock ownership. Study used secondary data in the analysis covering a period of 11 years from 2005 to 2015 which was exposed to sensitivity analysis using OLS regression. The results obtained from the models were presented in tables

The study found that the regression equations for the period 2005-2015 related financial performance of the companies to their ESOPS, company size and inflation. The study concludes that ESOPS have a strong positive and significant influence on the financial performance among listed firms in the NSE in Kenya. A recommendation for study is that companies' management should put in place and implement corporate policies in encouraging employees to take up the ESOPs among the companies listed in the NSE. This is by having a high-involvement and open culture necessary for ESOPs to thrive. The study also recommends that a public policy formulation encouraging investors and entrepreneurs to promote broad based ESOPs in their investments and enterprises. The policy also should facilitate employee buyouts scheme and business succession, a viable alternatives to divestures and spin offs.

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LIST OF ABBREVIATIONS

CMA	Capital Market Authority
ESOP	Employee Stock Ownership
EABL	East African Breweries Limited
ERISA	Employee Retirement Income Security Act
I&M Bank	Investment and Mortgage Bank
KCB	Kenya Commercial Bank
KPIs	Key Performance Indicators
NCEO	National Center for Employee Ownership
NSE	Nairobi Securities Exchange

CHAPTER ONE

1.1 Background of the Study

Employee Share Ownership Plans (ESOPs) has its origins in the United States of America (Hallock et al, 2003). Firms adopt ESOP to motivate employees to contribute in the capital of the company through stock ownership hence increasing employee organizational affiliation, performance and well being of the firm. (Parks, 1991; in Hallock, 2003).

Employee Share Ownership Plans is a qualified retirement scheme which is accompanied by a trust. (Parks, 1991). Specifically, he defined ESOP as a defined contribution plan that is a stock bonus plan or a qualified stock bonus money purchase plan that must invest primarily in qualifying employer securities.

Firms adopt ESOPs to encourage employee commitment which has been found to improve job contentment, psyche, and participation as Becker et al. (1996) postulated. Organizational commitment among employees is inversely related to turnover. The first ESOP was established in 1956 in the US. The Employee Retirement Income Security Act of 1974 (ERISA) set the ground on which the legal framework within which such plans would operate. In Kenya, ESOPs are recognized in the Income Tax Act Section 5 primarily as investment vehicles under the Capital Markets Act and many companies are now considering their potential benefits.

One of the benefits of ESOP adoption is increased financial performance of the adopting firms. It is in this light that the study aims to discern the effect of the adoption of ESOPs on the financials of firms listed in the NSE.

1.1.1 Employee Share Ownership Plans

Employee Share Ownership Plans (ESOPs) have been defined differently by several writers. ESOP is a qualified retirement scheme which is accompanied by a qualified trust. (Parks, 1991). Specifically, he defined ESOP as a defined contribution plan that is a stock bonus plan or a qualified stock bonus money purchase plan that must invest primarily in qualifying employer securities.

An ESOP is an arrangement between an employer and worker in which the worker is granted privilege to own defined quantity of shares in the firm, usually discounted and upon attainment of agreed key performance indicators (KPIs). (George Deeb, 2016)

There are two types of ESOPs; Leveraged and unleveraged. In leveraged, the ESOPs sources for funds to buy stocks and the stock is kept into an employee stock ownership trust (Bartkus, 1997), having overall oversee up to when the borrowed money is repaid while in latter employees buy shares with money from their own sources. Both of these forms may be started by employers or the owners.

There are various forms of ESOPs; Non-Qualified Stock Option Plans can be owned by anyone be it employees, directors or partners .In addition they can be exercised anytime , is taxable on the recipient if the offer price is less than fair market value (George Deeb,2016)

While in Qualified Incentive Stock Option Plans it's only the employees who qualify for this scheme. Waiting period is one year to exercise. May not be transferred to anyone (George Deeb, 2016)

Phantom Stock Option Plans are issued when the founders do not want any saturation to their shares. Instead, they give incentive to their workers by conferring them equivalent financial value they would have got by possessing the stocks. Such a case, the firm will incept a Phantom Stock Option Plan. Contrary to being given mandate to buy stock, the employees have the mandate to get the same economic value they would have made by owning the stock, in lie of owning the shares. (George Deeb, 2016)

ESOPs are the results of choices and outputs of wholly taken by the owners. (Gordon and Pound, 1990:528 cited in Bartkus, 1997). ESOPs adoption offers employees an opportunity to participate in the ownership and also participation in decision-making as noted by Hallock *et al*, (2003).

The concept of ESOPs has long history in the United States of America (Hallock et al, 2003). The motive of the ESOPs was to motivate employees partake in the capital contribution of the company by share ownership, thereby employee affiliation, attachment and seamless relationship between labour and the owners of the company (Parks, 1991).

Scholars have written about the reasons for the rise in the adoption of ESOP's by corporations and entities in the United States of America. Employee affiliation and attachment is the prime reason for work contentment, high-spiritedness and low absenteeism (Becker et al. 1996).

Mathieu and Zajac (1990) and Meyer et al. (2002) concur that firm affiliation and attachment is inversely related to turnover or even nonexistent in employees highly attached to the firm they work for. Workers who show great attachment and affiliation towards the company they work for have their needs in tandem to those of the employer hence the agency cost attributable to company worker is minimized (Brown et al. (2011). ESOPs satisfy a couple of company motives amongst others providing corporations with beneficial deductions like tax (Pugh *et al.*, 2000).

Douglas Kruse and Joseph Blasi (2013) concurred that ESOPs adoption give rise to sales and employment. They further observed that, firms that have adopted ESOPs have a high probability of being in business a couple of years afterwards.

In the emerging markets like India, the concept of ESOP has continued to be on the rise. ESOPs studies in India are not as old as of the USA. ESOP however, became popular as ephemeral inducement due to the upsurge in share prices in the Information Technology sectors during the years of 2000 (Dhiman, 2008). However, the author further notes that no certain exists between ESOPs and performance of the firm.

In Africa, specifically South Africa, ESOPs have been used over time as employee benefit schemes and to promote staff empowerment programs. Locally in Kenya, ESOPs are becoming increasingly popular as investment vehicles in the local market as schemes to provide employees with the opportunity to acquire or purchase shares in the company.

ESOPs are recognized in the Income Tax Act Section 5 as investment vehicles under the Capital Markets Act and many companies are now considering their potential benefits. Thus, the adoption of ESOPs by both private and public listed firms has been on the rise in Kenya in recent years.

The companies in Kenya have utilized the ESOP concept in an effort to attract and retain top talent, as a retirement plan and also generate funds in the Stock Exchange. In Kenya, shares are allocated to ESOPs trusts and these are to vest to employees over a given period of time depending on the stipulated conditions as detailed in the various ESOP Trust Deeds.

Examples of firms that have adopted ESOPs include KCB Bank Limited, Equity bank, NBK, EABL, Safaricom, Kenol Kobil, Scan group and Housing Finance Corporation Limited.

1.1.2 Financial Performance

Financial performance refers to measuring the results of operations and policies in financial terms. The concept of financial performance was nurtured by French (1987) controvverted that workers will perceive approach ownership method an investment anticipation. The opinion is also congenial to Jensen and Mecklings (1976) agency theory that monetary inducement like woker possession of stocks realigns their interests with those of the owners.

NCEO (2010) noted employees who participated in ESOPs do well. Employees accrued higher wages and their retirement assets almost tripled compared to employees work in firms that have not adopted ESOPs.

The study will measure financial performance in terms performance efficiency ratios like assets turnover, operating profit margins and operating profits relating to assets.

These efficiency ratios are attributed to indirect improvement in the firm's performance as a result of change of worker's views of being part of the ownership structure of the firm thereby inducing them to be accountable and fruitful.

1.1.3 The Effect of ESOPs on the Financial Performance

Results of research coupling ESOPs with firm financials are varied. Some studies have indicate a positive impact while others have indicated a negative or nearly no relationship. The conclusions of the major studies have foraged relationship of ESOPs adoption verses firm performance, the worthwhile of the firm and share profitability show that the impact of adoption of ESOP on the firm performance appears not strong; however a positive relationship is present.

Studies on the ESOPs indicate that that financial result will be affected by the inception of an ESOP in more ways than one. ESOPs boost employee morale and leads to good employee

behavior and perceptions leading to attractive firm outcomes in form of profitability and customer contentment (Daniel Koys, 2001)

According to Pierce, Kostova, and Dirks (2001), ESOPs instill feeling of obligation including the investing resources and time to amongst others to propagate vision of the company, being concerned on how the firm performs. Employee will have a close relationship with the company akin to egoistic ownership; a quest to propagate firm's performance. Secondly, workers may increase performance ratios resulting from the concept opposite monitoring of managers by the new owners. (Pugh *et al.*, 2000).

Other writers have however indicated that ESOPs impede the efficient transfer of corporate control leading to the shareholders loss of potential takeover premium and also excessive consumption of firm resources by entrenched managers, thus leading to less than optimal performance by the firms.

1.1.4 Firms in the NSE that have Adopted ESOPs

Nairobi Securities Exchange (NSE) is categorized into twelve market sectors. The sectors include agricultural, automobile, banking, commercial and services, Construction & Allied, Energy& Petroleum, Insurance, Investment, Investment services, Manufacturing & Allied, Telecommunication & Technology and Real Estate Investment trust. (NSE, Website)

The firms that have adopted ESOPs in Kenya include KCB Bank Limited, Equity Bank Limited, I&M Bank Limited, Housing Finance Corporation Limited, Kenol Kobil , East Africa Breweries, Safaricom , Access Kenya and Scan group Ltd.

Owing to high number of firms in the NSE that have adopted it presents an opportunity to study the effect, of these ESOPs on overall firm performance. The NSE has been selected as a focus of this study owing to the availability of secondary data for all the firms listed on the NSE hence easier to collect the data and the data will also be very reliable.

1.2 Research Problem

Employee Share Ownership Plans (ESOPs) is a definite contribution schemen that invests primarily in qualifying employer securities. Limited stocks, stock choices and stock capital appreciation entitlements. The adoption of ESOPs has continued to grow globally especially in

the developed world. The dramatic growth has been attributed to various factors such as tax benefits, mergers, acquisitions and employee benefits (Pugh *et al.*, 2000) and employee motivational tool (Dhiman 2008).

The NSE has a couple of firms that have adopted ESOPs in Kenya. Thus the need of establishing the impact of ESOPs adoption on performance of firms in the NSE. Little research exists on study of it to establish effect of adoption on financial performance. Nkubitu (2013) concluded that ESOPs have a strong positive influence on the monetary performance on companies in the NSE in Kenya. However, its limitation is in time under study, the research was only done for three years hence the need for a longer period for study. Odero (2012) in his research indicated that adoption of ESOP had a substantial influence on impact on the firm's performance while for other firms adoption of ESOP did not exhibit a tangible effect on financial performance of the firms.

As a result of the study limitations on existing studies done on ESOPs effect on financial performance hence the need to increase time frame of the research study to 10 years (2005-2015) The mixed results from the previous research and short period under consideration informed the study which answers this research query: Does the adoption of ESOPs by firms listed in the NSE have an impact on the financial performance?

1.3 Research Objectives

The purpose the study at hand is to establish the impact of adoption of ESOPs verses the firm's performance of firms that are on the bourse. In specifics, study addressed the following purpose; To investigate the effect of ESOP adoption on the firms' performance listed in the NSE.

1.4 Value of the Study

This study purposes to provide insights into the effects of adoption of the ESOP and firm performance in financial sector.

At the Organizational/ institutional level, this study provides information to the companies which are trying to retain their valued top talents at the institutions. Many institutions today are facing the challenges of acquiring and keeping the young generation employee a work since majority as

spending considerably fewer and fewer years at one employer. (*Business Daily*, Friday August 5, 2011).

The research would inform policies in regard to the taxation and investment on ESOPs. Attracting and retaining innovators with adequate equity based compensation would be appropriate going forward.

Finally, the study makes a contribution into the body of research undertaken on the impact of adoption of ESOP on firm's performance that are in the NSE.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Three sections are presented in this chapter. The first section reviews the theoretical framework on which the study is based. The second section espouses on the reasons for the adoption of ESOPs by the firms. Section three covers the empirical reviews, that is, the literature that examine on the relationship between adoption of ESOPs by firms and firms' performance.

2.2 Theoretical Literature Review

The link of ESOPs adoption and the firms' attainment of financial goals is viewed in terms of agency, Stakeholders, Social Exchange and Incentive Contract Theories.

Agency theory posits that companies that are publicly held are faced with costs to ensure that the companies are run in accordance to motive of maximizing shareholders wealth. The costs are incurred by owners of the companies since they rely on managers of the firm to prioritize on projects that add value to the shareholders. As a result segregation of owners and controllers thus exist .How far the managers endeavor to maximize on wealth generation depends on the level of equity shareholding that is existing (Jensen and Meckling, 1976).

Stakeholder theory is intended to explain operations of established corporations. (Thomas and Preston, 1995). Adoption of ESOPs in a firm can be viewed to be in line with the stakeholder's theory as far as satisfaction of multiple stakeholder interests in the firm are concerned.

Social-exchange theory contends that if the act done by one person to the other is valued by the recipient, the more appreciative he gives in return. (Homans , 1958). The position espoused means companies that give generous reimbursements stand a higher chance to acquire and maintain employees for there skills to be harnessed for sake of attainment of company objectives.

Incentive Contract Theory contends that there exist information asymmetry between the management and the employees which when tapped can be beneficial to the management. (Levine & Tyson, 1990). As such, adoption of ESOPs is regarded as way of reducing the information asymmetry.

2.2.1 Agency Theory

Agency theory contends that the firm owners bear expenses by hiring people who manage the company affairs. The expenses are evident in perquisites given to the runners of the company and even in form of below par decisions made regarding the operation of the firm. The firms that managers are in charge tend to concentrate on increasing sales instead of profits and the rate of profit is low and invariable and more so the engage in earnings management (Smith 1976; Nyman and Silberston, 1978; 1981 in Pugh et al, 2000). Such activities shift affluence from the people who own the company the managers are limited through checks and balances. As a result, managers skewed way of business operations and deployment of resources sub optimally erodes shareholder wealth value.(Fama & Jensen, 1983).

Expectedly, increasing employee ownership comes about as result on ESOPs which increases owners, albeit internally. If the owners brought on board have substantial powers for making decisions ,it presupposes that courtesy of agency theory the firm's performance improves accordingly.

By contrast, if the new owners on the block who couples up as employees have no powers for decision making means the existing managers prior to the ESOPs will have more control. To greater extent the new owners will endeavors to be in good terms with the existing managers for the sake of their job security.

Consequently, agency theory posits that ESOPs adoption encourages more management monopoly thereby begetting less corporate performance. (Chang & Mayers, 1992). Employees taking up ESOPs likely do not gain commensurate decision ability. Some noted difference in the employee's behaviors could be as a result of other more tangible inducements to perform since they stand to accumulate personal wealth.

Pugh et al (2000) observed an alternative view by assuming that the ESOP shares are indeed 'ally' shares, ESOPs tends to increase the voting power of the management. In case of a hostile

takeover the management has a vantage position to elicit high price thereby making it beneficial to the wealth of the shareholders.

2.2.2 Stakeholders Theory

Stakeholder's theorists propose that all people who are affected by the operations of the firm and have honest desires in the enterprise existence and their desires are honest there exists no pecking order over each other's desire.

This theory guides the structure and operations of established corporations. (Thomas & Preston, 1995). They observed that stakeholder's theory is general and comprehensive and goes well beyond the descriptive observation.

Clarkson (1991) and Halal (1990) noted in their empirical studies that the management may not explicitly stick to this theory but they are cognizant of the fact that the operations of the firm and decisions made affect all people who are affected by the existence and operation of the firm.

Evan and Freeman (1993) observes that the management is obligated to take care of the welfare and interests of diverse parties and ensure an amicable position where interest maybe conflicting. They also concluded that the corporate performance test will be satisfying the interest of various parties instead of steering the firm purely for financial purposes. ESOPs adoption can be viewed to be in line with the stakeholder's theory as far as satisfaction of multiple stakeholder interests in the firm are concerned.

2.2.3 Social Exchange Theory

Social-exchange theory contends that if the act done by one person to the other is valued by the recipient, the more appreciative he gives in return. (Homans , 1958). The position espoused means companies that give generous reimbursements stand a higher chance to acquire and maintain employees for there skills to be harnessed for sake of attainment of company objectives.

Several studies contend that benefits are a useful means to motivate, retain and attract qualified employees (Kurlander & Barton, 2003). In addition, there exist firms providing beneficial opportunities to employees for skills development and enhancement in order to make th workforce more skilled and strengthened. (Cantoni, 1997).

Employee benefits play a role in acquiring and maintaining quality employees who are a vintage resource to the firm thus providing a cutting edge to the firm (Horwitz et al., 2003). The overall appeal of organizations can be enhanced through beneficial inducements offering making employee be more affiliated and attached to the firm. Consequently, greater effort and productivity will be realized. In a nutshell, more commensurate benefits will improve firm productivity by acquiring and maintaining quality labor. (Lipold, 2002).

2.2.4 Incentive Contract Theory

Incentive contract theorists ponders the reason for employees putting much effort into work while their output may not be fully be quantified and also how they are encouraged to put forth ideas on how productivity of the firm can be enhanced since they are key cogs in the conveyer belt of the production process. (Lazear, 1986).

Various inducement programs exists that can be incepted by the management though they have varied outcomes. The inducement programs exist to create a perfect information environment in which employees are aware of what is at stake to benefit. The dilemma on how to effectively encourage and spur performance is crucial more than ever before since the greater levels of information exists within the employee themselves. (Levine & Tyson, 1990).

Milgrom and Roberts (1992) suggested that, the principle of owning property rights is critical to make and develop assets. The technical aspects of owning is having absolute right to make decisions involving use of an asset and right to revenues after all the encumbrances are settled. These two factors combined provide the impetus to ownership and is the decisive combination since decision maker faces the financial consequences of the decision's results.

2.3 Reasons for Adoption of ESOPs

This section looks at different reasons for establishing ESOPs. The main reason for adoption of ESOP is for exclusive benefit of participants. Freeman and Knoll (2008), argues that ESOP is an employee benefit plan and therefore must aim at benefiting participants financially.

A survey of Ryterband (1991) and Pugh *et al.* (2000) postulated that firms that had ESOs showed that firms' employees recorded various perceptions towards ESOPs including morale boosting, ultimately saving on taxes ,surge in employee productivity, reduction in employee severance with the company and capital source to the firm.

Adoption of ESOPs encourages employee attachment and retention which influences job contentment, encouragement and reduces absenteeism. (Becker et al. 1996), and Daniel Koys (2001) observed that good perceptions of employees results into satisfaction of customers and profitability improvement.

In addition, adoption of ESOP is expected to lead to increased employee motivation and productivity. This could be attributed to ownership benefits of the ESOP to the participating employees. Buchko, (1992) in Bartkus (1997) indicated in their study that employee's who coupled up as owners of the firm and viewed ESOPs as gateway for them to a greater say in running of the company and in decision making made them more attached to the company ,felt more contented and they were more actively involved in their work. This is consistent with the agency theory, which indicated that providing ownership interest spurs interest in employees by taking into consideration their interest in the same wavelength as that of other shareholders (Chen & Kensiger, 1988)

ESOPs are adopted as a defense against hostile takeovers. Regardless of the reason behind the ESOPs implementation, ESOPs act as protection against unfriendly take overs since a substantial large votingbase is in the employees of the ESOP firm who on the same page as the management. (Pugh et al, 2000). Stulz (1988) in Adamson (1993) also contended that ESOPs provide additional voting power to incumbent managers who can then extract a higher price for the firms' shares from potential bidders than can less informed outside shareholders.

ESOP can be used for in a various reasons such as staff retention, business restructuring and expansions. Additionally, ESOPs are used as a common strategy in business as result for cut throat competition for gifted professionals. Thus, they act as bait to attract, acquire and encourage gifted personnel. They thus enhance business operations (Chen Wei- Ning & Chen-Yi Hsu 2008), leading to avenues for business restructuring and expansions.

ESOPs enhance firm stability and survival rate (Blair, Kruse, & Blasi 2000). The perpetuity of the ESOP firms is higher than to non-ESOP . They argued that ESOPs reduced the cost of investing weighted average capital thus value adding to the firm.

2.4 Empirical Review

Studies have been done on the linkage on ESOPs inception and the added value to the firm, however, outcomes on the actual effect on the ESOPs is varied (Ivanon and Zaima 2011; Hallock *et al.*, 2003). This is allusion to studies conducted by different scholars in different parts of the world.

Blassi and Krusse (2002) have conducted several studies to address the issue of whether the employee ownership affects firm performance. In these studies, they have severally compared to the ESOP firms' performance with non ESOP firm in the studies. Their conclusions are largely either favorable or unfavorable and some even neutral.

Gupta and Dhiman (2010) conducted an ESOP study on the firms in the pharmaceutical industry in India geared towards measuring the after ESOPs implementation performance of the companies. Study examined 10 of the top pharmaceutical companies that adopted ESOP during the years 2000 to 2005 and using the financial performance measures for six years (beginning from 2006 to 2010) after following the company's adoption of ESOPs. The companies post financial performance was measured by four financial ratios: Net profit ratio, Employee cost ratio, Material Cost Ratio and Administrative cost ratio and these were compared against industry average. The empirical results of the study indicated mixed results. Some companies' financial performance improved marginally compared to average in the economy on all financial parameters while one company's the performance reduced compared to the industry average.

Similarly studies conducted on the impacts of ESOPs on risk and performance of the companies whose stocks were trading in the French stock exchange also revealed mixed results (Stephane and Henri, 2002). The Study majored on the linkage of ESOPs and company results for the firms listed in the French stock exchange. In the study, 221 firms were examined which had ESOPs from a total sample of 701 publicly listed companies in Paris Security Exchange. The relationship existing between ESOPs and financial indicators were studied for the year 2000. They examined the correlation between ESOPs and risk and performance indicators, while controlling for size, sector, age and leverage.

The empirical results for this study turned out to be consistent with the agency theory predictions, where ESOPs mechanism was expected to align the employee and shareholder interests. Overall, however, the study did not observe any optimal threshold of employee

ownership which might maximize performance. The Study also noted that the presence of ESOPs is positively correlated to performance, but the relationship of causality remained complex and that ESOP firm had a higher beta.

Hamid and Iqbal (2000) conducted studies on the price of the stock and performance of the firms that have ESOPs. The ESOP firms sample was obtained from National Centre for Employee Ownership (NCEO), in USA. They explored the financial context of ownership by employee by delving into the linkage of returns on the stocks and profitability of the ESOP adopted firms. They noted that prices of stock had an impact on accounts of ESOPs which consequently impacts on company affiliation and output levels of employees. They hypothesized that employees in the ESOP firms will show more affiliation and output levels will peak when the prices of stocks rises and lowly affiliated when the prices of stocks decline. A sample of 76 listed firms that had operational ESOP schemes on or before 1988 tested the hypothesis. They constructed a manipulative sample by corresponding firm that had adopted ESOP with one that had no ESOP but were similar in size a year before the ESOP adoption. Findings of this study were unvarying with other findings of past studies that showed results of the firm improved on inception of ESOP schemes. Similarly, based on these studies, it was expected that results of firm with ESOP scheme will be poor on prices of the stock falling. However, results were anomalous in this study for the ESOP firms that experienced falling stocks prices as they also showed improved performance.

The studies above have indicated mixed results with positive association of the effect of ESOP adoption and corporate financial performance. However, there are some studies that show negative relationship between ESOPs adoption and firm performance as noted below.

Blasi et al (1996), in their study of the monetary returns of ESOP companies that had gone public on effects of investors and management, noted that returns of publicly quoted companies that sponsored ESOPs were marginally more than those of similar firms but did not have ESOPs. Study had control environment for firms whose financial risk and company size was noted to have independent of financial performance. The study comprised of more than 9,000 active companies with fiscal year end in between 1981 to 1993 and financial data obtained from the data base. The components for analysis included information such as return on capital invested, debt level, the value of shares in the bourse, employees number and if the company had an

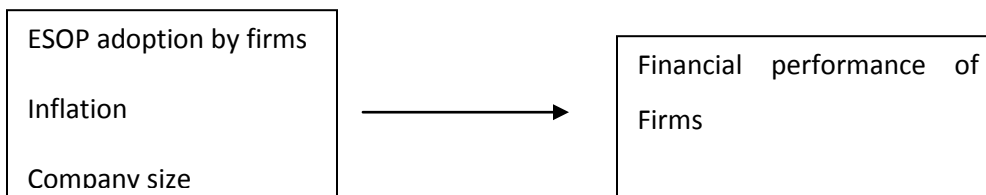
operational ESOP in the year and if so its value. Findings for this study noted that effects of ESOPs was insignificant for the companies that were small but for large companies the effect was very significant.

Explanation put forth was that publicly quoted companies with ESOPs are an exclusive group of good profitable firms that the owners are ready to sacrifice return on finances to achieve other set of objectives. The conclusions for the study indicated that ESOP companies had higher returns compared to non ESOP companies. Furthermore, ESOP firms, particularly the ones that had employees less than 500, had at did not have ESOPs.

2.5 Conceptual framework

Independent variables

Dependent variable



The relationship of ESOPs adoption and the firm performance can be examined in terms of agency theory, Stakeholders Theory, Social Exchange Theory and Incentive Contract Theory

Agency theory contends that the firm owners bear expenses by hiring people who manage the company affairs. The expenses are evident in perquisites given to the runners of the company and even in form of below par decisions made regarding the operation of the firm. The firms that managers are in charge tend to concentrate on increasing sales instead of profits and the rate of profit is low and invariable and more so they engage in earnings management (Jensen and Meckling, 1976).

Stakeholder's theorists propose that all people who are affected by the operations of the firm and have honest desires in the enterprise existence and their desires are honest there exists no pecking order over each other's desire.

This theory guides the structure and operations of established corporations. (Thomas & Preston, 1995). They observed that stakeholder's theory is general and comprehensive and goes well beyond the descriptive observation.

Social-exchange theory contends that if the act done by one person to the other is valued by the recipient, the more appreciative he gives in return. (Homans , 1958). The position espoused means companies that give generous reimbursements stand a higher chance to acquire and maintain employees for their skills to be harnessed for sake of attainment of company objectives.

Incentive contract theorists ponders the reason for employees putting much effort into work while their output may not be fully be quantified and also how they are encouraged to put forth ideas on how productivity of the firm can be enhanced since they are key cogs in the conveyer belt of the production process. (Lazear, 1986).

Adoption of ESOPs in a firm can be viewed to be in line with stakeholder's theory as far as satisfaction of multiple stakeholder interests in the firm are concerned. While it can be in line agency theory where agency costs need to be minimized and social exchange theory where more voluntary compensations have a higher chance of attracting and maintaining skilled and knowledgeable employees.

ESOPs adoption realigns employees' objectives as those of the firm and at same time employees being one of the core stakeholders of the company when well compensated top talent can be attracted and retained.

2.6 Chapter Summary

A couple of research on employee ownership shows positive effects on financials at the level of the firm. These studies show that the firms that are owned by employees have high profitability and productivity level, they survive longer, and posts higher shareholder returns. Comparatively, after adoption performance of firms is better than before adoption. Whilst some researchers found an agreeing relationship between ownership of firm and performance of firm, other studies reported no relationship between employee ownership and financial performance. Most of these studies are done in other countries whose financial setting, competitive and strategic approach is different from that of Kenya. This study, therefore, seeks to fill this gap by focusing on the effect of Employee Stock Ownership Plans on financial performance of companies listed in the NSE.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents methods employed during the research. Divided into four sections where section one illustrates the design of the study, section two discusses the population under the study, the third section majors on data sources and actual data collection process while the fourth espouses on data analysis.

3.2 Research Design

The chapter brings out the methods employed to conduct the study specifying showing procedures required to obtain the facts needed to frame and elucidate the research problems (Birks & Malhotra, 2003).

The study adopted a descriptive survey design. Being the present oriented research that seeks to accurately describe the situation like it is and collection of data for the hypothesis to be tested

Descriptive research design was chosen because it encompasses collection of data, describing episodes and putting them into tabulations to enumerate collection of data. Description was used as mechanism for data analyzing to facilitate pattern establishment for drawing analysis. Through descriptive this data is reduced into manageable forms. (Glass & Hopkins, 1984).

3.3 Population

Mbokane (2009) refers to the population as sum of all members conforming to a set of particularization. Research population is generally a large assemblage of characters that are the main concern of a research question. (Castillo (2009). The population generally derives benefit from the research done.

In this the study, the research population is all firms listed in the NSE that had adopted ESOPs. There were 8 firms listed in the NSE that had adopted ESOPs (NSE Website).

3.4 Data Collection

Data collection will involve gathering information to address the research question at hand. For this study, secondary data, which refer to the information obtained from articles, books, newspapers, internet and magazines (Irerri, 2006), was collected. This data was used for generation of information and as Cooper & Schindler (2003) put forth. Secondary data is a calculable technique for assessing historical information amongst others, public records, report, government documents and opinions.

Data is collected from the Capital Markets Authority, respective company premises or their websites. The data collected covered periods between 2005 to 2015 for firms that have listed in the NSE and had adopted ESOPs between the periods. The study sought to determine whether adoption of ESOPs impacts firms' financial performance listed in the NSE.

Financial performance measures used is ROA. This is the recompense on assets and is measured by net income before extraordinary items divided by total assets. This ratio measures how effectively the firm generates after tax income from available assets.

3.5 Data Analysis

EvIEWS were used in data analysis. Study is descriptive in nature; both quantitative and inferential determination was employed analyzing data. Data was run through various regression models so as to clearly bring out the effects of change in ESOPs on firm's financial performance. The result obtained from the models was tabulated to aide in the deciphering and drawing the inferential statistics.

Conceptual model below, which has been used by previous scholar such as Kramer (2008), was tested:

$$FP = f(ESOP) \dots\dots\dots (1)$$

The empirical model based on the variables above is:

$$Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \epsilon \dots\dots\dots (2)$$

Where: Y = Financial performance (measured by Return on Assets)

β_0 = Constant Term;

$\beta_1, \beta_2, \beta_3$ = Beta coefficients;

X1= ESOPS (measured by Number of ESOPS/Total number of shares)

X2=Company size (measured by natural log of Total assets)

X3= Inflation (Consumer price index)

ε = Error term

A similar Regression model was adopted by Pugh et al (2000) in a study conducted to determine how ESOPs adoptions impact firm performance in the American Industry where they deduced that ESOPs resulted in improvements in morale and job satisfaction which promoted the general output and cutting edge of the American industry.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

The chapter presents results processed from collated data during study on effect of employee stock ownership plans on financial performance of firms listed in NSE. The sample encompassed nine listed firms in the Nairobi Securities Exchange for the period (2005-2015). The findings of the study are presented per year from 2005 -2015.

4.2 Regression Results

The study conducted a cross-sectional OLS multiple regression on the selected independent variables between 2005 and 2015 and results of financial performance.

4.2.1 Year 2005 Analysis and Interpretations

The coefficient of determination elucidates the degree of which dependent variable variation can be accounted for in the change of independent variables. The dependent variable in this study is performance of firm in monetary terms while ESOPS, company size and inflation represent independent variables.

Table 4.1: Coefficients of 2005 Model

Var.	Co-eff	Sd. Error	t-St	Prb.
CONSTANT	-118983	0.021297	-5.586882	0.0113
ESOPS	738206	0.066512	11.09878	0.0016
COMPANY-SIZE	62207	0.042529	1.462710	0.2397
INFLATION	-69050	0.001108	6.232496	0.0083
R2	0.976782	Mean dependentvar		0.027856
Adj. R2	0.953565	S.D. dependentvar		0.013800
S.E. regression	0.002974			

The data findings from 2005 market statistics were analyzed using the Eviews and output presented in table 4.1. The results of the Eviews output were put in the regression equation and below results were realized;

$$FP = -118983 + 738206ESOPS + 62207 CS - 69050INF$$

According to the model, ESOPS and company size were positively correlated with financial performance while inflation was negatively correlated with financial performance. From the model, taking all factors that is ESOPS, company size and inflation unchanged at zero, performance financially measured will be -118983.

The findings shows, if all factors are held unvaried at zero, an increase in ESOPS by one will results into a 738206 financial performance increase. Increase in company size by one unit will result make greater performance of firm by 62207 while a unit increase in inflation results into a 69050 decrease in performance of the firm. This infers that ESOPS had more effect on financial performance followed by company size while inflation had a negative effect.

4.2.2 Year 2006 Analysis and Interpretations

Table 4.2: Coefficients of 2006 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	62778	0.012402	5.061871	0.01242
ESOPS	452470	0.467033	-10.38999	0.00611
COMPANY SIZE	680637	8.075144	8.421691	0.00752
INFLATION	-34490	0.008619	4.001548	0.01559
R-squared	0.991428	Mean dependent var	0.011133	
Adjusted R-squared	0.965712	S.D. dependent var	0.115186	
S.E. of regression	0.021329	Akaike info criterion	-4.866948	

The data findings from 2006 market statistics were analyzed using the Eviews and output presented in table 4.2. The coefficient table in table 4.2 shows results that were used to obtain the below model;

$$FP = 62778 + 452470 ESOPS + 680637 CS - 34490INF$$

According to the table, the financial performance had an autonomous value of 62778 that is when the value of all the variables in the study that are independent are held at variables zero. A unit increase in ESOPS increases the financial performance by 452470 when the company size and inflation variables are held constant. A unit increase in company size, holding other variables constant, increased the financial performance by 680637. A unit increase in inflation, holding other variables constant, decreased the financial performance by 34490. This shows that ESOPS and company size had a positive relationship with the financial performance while inflation negatively influenced the companies' financial performance.

4.2.3 Year 2007 Analysis and Interpretations

Table 4.3: Coefficients of 2007 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	61486	0.061179	1.005007	0.03718
ESOPS	4776963	2.472882	-1.931739	0.01256
COMPANY SIZE	5638128	4.342994	-1.298212	0.02640
INFLATION	-870942	0.027390	0.317969	0.04664
R-squared	0.696268	Mean dependent var		0.007465
Adjusted R-squared	0.588469	S.D. dependent var		0.147168
S.E. of regression	0.138176	Akaike info criterion		-0.813727

The data findings for 2007 were computed, analyzed and presented in table 4.3 above. From table 4.3, the regression model is presented below:

$$\mathbf{FP = 61486 + 4776963 ESOPS + 5638128CS - 870942INF}$$

According to the regression model, when the values of ESOPS, company size and inflation are zero, financial performance will be 61486. When ESOPS is increased by one unit, the financial performance will increase by 4776963 while when company size is increased by one unit, the financial performance will increase by 5638128. The financial performance will also decrease by 870942 when the inflation is increased by one unit holding other factors constant. This shows that in this year, ESOPS and company size had a positive correlation with financial performance while inflation had a negative effect.

4.2.4 Year 2008 Analysis and Interpretations

Table 4.4: Coefficients of 2008 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	232172	0.106096	2.188326	0.08023
ESOPS	413643	0.555983	0.743985	0.04903
COMPANY SIZE	287309	0.269351	-1.066673	0.03349
INFLATION	-90300	0.006817	-1.324548	0.02426
R-squared	0.734530	Mean dependent var	0.049927	
Adjusted R-squared	0.655248	S.D. dependent var	0.029290	
S.E. of regression	0.025277	Akaike info criterion	-4.216747	

The data findings from 2008 market statistics were analyzed and the Eviews output presented in table 4.4 above. The coefficient table in table 4.4 above employed to come up with the below model:

$$FP = 232172C + 413643 ESOPS + 287309 CS - 90300 INF$$

According to the model, only ESOPS and company size were positively correlated with financial performance while inflation was negatively correlated with financial performance. From the model, taking all factors (ESOPS, company size and inflation) unchanged at zero, financial performance of the firm will be 232172. Data analyzed shows that when independent variables at zero, a unit increase in ESOPS will lead to a 413643 increase in financial performance. A unit increase in company size will lead to a 287309 increase in financial performance while a unit increase in inflation will lead to a 90300 decrease in financial performance. This infers that ESOPS had more effect on financial performance followed by company size while inflation had a negative effect.

4.2.5 Year 2009 Analysis and Interpretations

Table 4.5: Coefficients of 2009 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	403375	0.351464	1.147701	0.02948
ESOPS	316479	1.640839	-0.802321	0.04530
COMPANY SIZE	665730	0.998375	-1.668441	0.01463
INFLATION	91110	0.020464	-0.445245	0.04718
R-squared	0.796105	Mean dependent var		0.078073
Adjusted R-squared	0.594158	S.D. dependent var		0.093353
S.E. of regression	0.088849	Akaike info criterion		-1.714573

The data findings for 2009 statistics were processed using Eviews and the output presented in table 4.5 above. The regression model drawn from table 4.5 above is presented below:

$$FP = 403375 + 316479 ESOPS + 665730 CS + 91110 INF$$

According to the table, the financial performance had an autonomous value of 403375 that is when the value of all the independent variables is zero. A unit increase in ESOPS increases the financial performance by 316479 when the company size and inflation variables are held constant. A unit increase in company size, holding other variables constant, increased the financial performance by 665730. A unit increase in inflation, holding other variables constant, increased the financial performance by 91110. This shows that ESOPS, company size and inflation had a positive relationship with the financial performance.

4.2.6 Year 2010 Analysis and Interpretations

Table 4.6: Coefficients of 2010 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	334792	7.489009	-0.418586	0.04929
ESOPS	139758	2.398527	-0.892113	0.04132
COMPANY SIZE	746768	167.7076	0.445822	0.03744
INFLATION	-130200	0.032164	0.040487	0.02693
R-squared	0.799084	Mean dependent var		0.094183
Adjusted R-squared	0.681466	S.D. dependent var		0.109229
S.E. of regression	0.123649	Akaike info criterion		-1.041639

From the finding of the study on the 2010 market statistics as analyzed and presented in the table above, the following regression equation was established by the study for the year 2010:

$$FP = 334792 + 139758 ESOPS + 746768CS - 130200 INF$$

From the findings of the data it can be concluded that when the value of ESOPS, company size and inflation were zero, financial performance was 334792. The table also shows that holding company size and inflation constant, an increase by one unit of ESOPS increases financial performance by 139758, when other factors are held constant an increase in company size by one unit increases financial performance by 746768. If one unit of inflation was increased while holding other factors constant, the financial performance would decrease by -130200. This shows that the ESOPS and company size have a positive relationship with financial performance while inflation inversely affects companies' financial performance.

4.2.7 Year 2011 Analysis and Interpretations

Table 4.7: Coefficients of 2011 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	-1351255	1.999783	-0.675701	0.04292
ESOPS	1238832	1.910367	-0.648479	0.03453
COMPANY SIZE	1101328	12.37826	0.808941	0.04553
INFLATION	-121172	0.021619	0.054210	0.02589
R-squared	0.719283	Mean dependent var		0.085515
Adjusted R-squared	0.689148	S.D. dependent var		0.081191
S.E. of regression	0.084733	Akaike info criterion		-1.797515

The market data for 2011 was regressed on Eviews and the output presented in table 4.7 above.

From the data analyzed and presented in the table above, the model for the year 2011 is presented below:

$$FP = -1351255 + 1238832ESOPS + 121172 CS - 121172INF$$

According to the model above, holding ESOPS, company size and inflation constant at zero, financial performance will be -1351255. When the company size and inflation are held constant, a unit increase in ESOPS will increase the financial performance by 1238832. While when other factors are held constant, a unit increase in company size will increase the financial performance by 121172. The model also shows that inflation had a negative relationship with financial performance such that a unit increases in inflation holding other factors constant will lead to a decrease in financial performance of 121172. From the above model it can be concluded that ESOPS and company size positively influenced financial performance while inflation had a negative influence on the same.

4.2.8 Year 2012 Analysis and Interpretations

Table 4.8: Coefficients of 2012 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	1150972	13.46808	-0.854592	0.04318
ESOPS	2072553	1.962905	-1.055860	0.03394
COMPANY SIZE	1244396	141.0593	0.882179	0.04181
INFLATION	-69155	0.023142	-0.298795	0.04771
R-squared	0.704821	Mean dependent var	0.086331	
Adjusted R-squared	0.612286	S.D. dependent var	0.098250	
S.E. of regression	0.103620	Akaike info criterion	-1.395075	

The data findings for 2012 were computed, analyzed and presented in table 4.8 above. From table 4.80, the regression model is presented below:

$$\mathbf{FP = 1150972 + 2072553 ESOPS + 1244396 CS - 69155INF}$$

According to the regression model, when the values of ESOPS, company size and inflation are zero, financial performance will be 1150972. When ESOPS is increased by one unit, the financial performance will increase by 2072553 while when company size is increased by one unit, the financial performance will increase by 1244396. The financial performance will decrease by 69155 when the inflation is increased by one unit holding other factors constant.

This shows that in this year, ESOPS and company size had a positive correlation with financial performance while inflation had a negative correlation with financial performance.

4.2.9 Year 2013 Analysis and Interpretations

Table 4.9: Coefficients of 2013 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	2842081	4.116751	-0.690370	0.04207
ESOPS	1611070	1.194316	-1.348948	0.02352
COMPANY SIZE	5363988	70.36058	0.762357	0.04802
INFLATION	-47293	0.014183	-0.514227	0.01290
R-squared	0.718295	Mean dependent var	0.078704	
Adjusted R-squared	0.690727	S.D. dependent var	0.060219	
S.E. of regression	0.062891	Akaike info criterion	-2.393714	

The data findings for 2012 were computed, analyzed and presented in table 4.19 and 4.20 above. According to the ANOVA statistics in table 4.19 above, the model had a significance level of 0.049 which means that the model is appropriate to be used as a population parameter. From table 4.20, the regression model is presented below:

$$FP = 2842081 + 1611070 \text{ ESOPS} + 5363988 \text{ CS} - 47293 \text{ INF}$$

According to the regression model, when the values of ESOPS, company size and inflation are zero, financial performance will be 2842081. When ESOPS is increased by one unit, the financial performance will increase by 1611070 while when company size is increased by one unit, the financial performance will increase by 5363988. The financial performance will decrease by 47293 when the inflation is increased by one unit holding other factors constant. This shows that in this year, ESOPS and company size had a positive correlation with financial performance while inflation had a negative correlation with financial performance.

4.2.10 Year 2014 Analysis and Interpretations

Table 4.10: Coefficients of 2014 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	5753547	6.140631	-0.936963	0.03918
ESOPS	1299797	1.254566	-1.036053	0.03477
COMPANY SIZE	8589065	87.01430	0.987087	0.03689
INFLATION	-56154	0.014521	-0.423784	0.02893
R-squared	0.831004	Mean dependent var	0.081189	
Adjusted R-squared	0.670393	S.D. dependent var	0.063851	
S.E. of regression	0.066061	Akaike info criterion	-2.295386	

The data findings for 2014 were computed, analyzed and presented in table 4.19 and 4.20 above.

From table 4.90, the regression model is presented below:

$$FP = 5753547 + 1299797 \text{ ESOPS} + 8589065 \text{ CS} - 56154 \text{ INF}$$

According to the regression model, when the values of ESOPS, company size and inflation are zero, financial performance will be 5753547. When ESOPS is increased by one unit, the financial performance will increase by 1299797 while when company size is increased by one unit, the financial performance will increase by 8589065. The financial performance will decrease by 56154 when the inflation is increased by one unit holding other factors constant. This shows that in this year, ESOPS and company size had a positive correlation with financial performance while inflation had a negative correlation with financial performance.

4.2.11 Year 2015 Analysis and Interpretations

Table 4.11: Coefficients of 2015 Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CONSTANT	1194494	7.224585	-1.653374	0.01592
ESOPS	-772933	1.476519	-0.523484	0.04230
COMPANY SIZE	1822248	107.1565	1.700548	0.01498
INFLATION	-53206	0.016615	-0.192956	0.01546
R-squared	0.824239	Mean dependent var	0.100063	
Adjusted R-squared	0.778783	S.D. dependent var	0.082368	
S.E. of regression	0.079057	Akaike info criterion	-1.936187	

The data findings for 2012 were computed, analyzed and presented in table 4.19 and 4.20 above. From table 4.10, the regression model is presented below:

$$\mathbf{FP = 1194494 + 772933 ESOPS + 1822248CS - 53206 INF}$$

According to the regression model, when the values of ESOPS, company size and inflation are zero, financial performance will be 1194494. When ESOPS is increased by one unit, the financial performance will increase by 772933 while when company size is increased by one unit, the financial performance will increase by 1822248. The financial performance will decrease by 53206 when the inflation is increased by one unit holding other factors constant. This shows that in this year, ESOPS and company size had a positive correlation with financial performance while inflation had a negative correlation with financial performance.

4.3 Summary and Interpretation of Findings

From the above regression models for the eleven years, the study found out that there were several factors influencing the financial performance of companies listed in the NSE, which are Employee Share Ownership Plans (ESOPS), company size and inflation. The variables either influenced it positively or negatively. The study findings indicated that the intercept varied. The highest value was 5,753,547 and the lowest was -1,351,255 with an average of 960,496.27 for all years. The study also found out that the coefficient of ESOPS varied from positive to negative. The highest regression value was positive with an average coefficient of 1,116,985.27. This means that ESOPS positively influenced the financial performance.

The study found out that the company size varied in value although it was positive in all cases. This means that company size positively influenced the financial performance. The study further found out that the coefficients of the inflation to be negative in all the eleven regression models apart from 2009. This depicts that, according to findings, inflation negatively influences the financial performance.

The three independent variables that were studied (ESOPS, company size and inflation) explain only 71.56% of financial performance as represented by the average adjusted R² (0.7156). This

therefore means the three independent variables contribute about 71.56% of financial performance decision while other factors not studied in this research contributes 28.44% of the financial performance of companies listed in the NSE.

There has been several studies carried out on the effect of ESOPS on firms in different sectors but findings have to a large extent corroborated the findings on the effect of ESOPS on financial performance among companies listed in the NSE in Kenya. The study concludes that ESOPS have a strong positive influence on the financial performance among companies listed in the NSE in Kenya.

My results are consistent with prior research by Pugh et al. (2000) who observed that ESOPs are being used by corporate managers to take capitalize on tax benefits, boost short-term profits, or erect takeover barriers. Further, employee stock ownership is widely recognized as an effective tool of improving corporate performance by enabling employees to participate in the creation and sharing of wealth they create in an organization (Earl, 2000).

The study deduced that although the overall relationship between ESOPS and financial performance is positive, there are some cases showing negative relationship. Thus, the relationship between ESOPS and financial performance remains a controversial. This is in line with earlier studies that showed mixed results about the relationship between ESOPS and financial performance with few predicting a negative relationship (Pugh et al., 2000; Weston et al., 1990; Gordon and Pound, 1990; Lisa and Zwirlein, 1995) while other confirms positive relationship between inflation and financial performance (Blasi et al. 2003; Gordon and Pound, 2005). Even though these researchers have found a positive relationship between employee ownership and financial performance, other studies reported no relationship between employee ownership and financial performance. Kruse and Blasi (1997: 134-136) summarized eleven studies evaluating comparison of (a) performance before and after adoption of the ESOP, (b) ESOP to non-ESOP firms, and (c) post adoption performance of adopted ESOPS firms to matched non-ESOP firms. Most of the studies find small positive, but statistically insignificant effects.

From the findings, it can be observed that ESOPS affects financial performance positively. At any time a company issues ESOPS the employees and management will feel a form of ownership and will be more committed to their work leading to increased performance. However, the study

deduced that the dummy variable, company size positively influence financial performance while inflation negatively influence financial performance hence the conclusion of this study is that ESOPS and company size have a strong positive correlation with financial performance while inflation has strong negative correlation with financial performance. Therefore it will be important for a firm's management to understand the relationship that exists between ESOPS, company size and inflation and financial performance and the direction that they affect the level of financial performance for effective decision making.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Secondary data used in the analysis covered a period of 11 years starting 2005 to 2015. Population sample comprised firms listed in the NSE operating in Kenya in the study period. The screening process identified firms that had offered employee stock ownership plans were considered hence nine companies were identified for the study. The study sought to investigate the effect of employee stock ownership plans on financial performance of firms listed in the NSE.

Descriptive design was used during the study and the study used purposeful sampling to pick 9 companies listed in the NSE having employee stock ownership plans for the period (2005-2015) which was exposed to sensitivity analysis using OLS regression.

The study found that the regression equations for the period 2005-2015 related financial performance of the companies to their ESOPS, company size and inflation. From the above regression models for the eleven years, the study found out that there were several factors influencing that influenced financial performance of firms listed in the NSE, which are ESOPS, company size and inflation. These variables either influenced it positively or negatively. The three independent variables that were studied (ESOPS, company size and inflation) explain 71.56% of financial performance as represented by the average R².

The study concludes that ESOPS bear a strong positive and significant effect on the financial performance of the listed firms in the NSE in Kenya. The recommendation for the study is that the companies' management should put in place and implement company policies that encourages employees to take up the ESOPs among the companies listed in the NSE. This is by having a high-involvement and open culture necessary for ESOPs to prosper. The study also recommends that a public policy formulation encouraging investors to promote broad based ESOPs in their investments and enterprises. In addition, the policy also should be geared towards facilitating employee buyouts scheme and business succession, a fruitful alternatives to selling the company to an external buyer.

5.2 Conclusions

This paper examines the effect of ESOPs on firm's performance among firm's on the NSE bourse in Kenya. The study concludes that ESOPs have a strong positive influence on the financial performance among companies listed in the NSE in Kenya. ESOPs are used for many reasons, including providing for a tax-favored, flexible transition of ownership in close knit held companies and as a means of providing an additional incentive that ties employee and firm's interests together. ESOPs are adequate methods of spurring firm performance by facilitating employees to engage in the formation and partaking of wealth they create in an organization. Additionally, it improves r employee morale and satisfaction.

Employees, if accorded the ownership state in the firm, they would have the impetus to increase their output levels and performance, hence promoting the overall productivity and competitive edge. ESOPs are used by the management to seize beneficial tax deductions and upraise takeover defenses.

The study deduced that although the overall relationship between ESOPs and financial performance is strong and positive, there are some cases showing negative relationship. Thus, the relationship between ESOPs and financial performance remains a controversial. These shows there are mixed results about the relationship between ESOPs adoption and financial performance with both a negative relationship and unequivocal relationship of ESOPs and performance of the firms. This also points to non linear relationship existence between these two variables. Buttressing the findings in the past researches such as Conte et al. (1996), the study depicts further uncertainty on the purported role of ESOPs in providing useful employee incentives. Our finding, on the other hand also, supports contract theory that highly diffused ownership does not give meaningful work incentives. Because equity shares under an ESOP are typically allocated to a high number of employees, such plans are likely to incur a serious free-rider problem and hence are dysfunctional in motivating employees. The purported benefits of an ESOP are attainable in organizational in which the incentive based productivity performance link is more easily observable by the participating employees. ESOPs from a firm's perspective can bring increased customer and employee attraction rates, talent retention and employee motivation. Such recognition relies on more than quick fix perks.

5.3 Recommendations for Policy and Practice

The study established that ESOP have a significant influence on the financial performance, CMA should consolidate policies that encourage the adoption of the ESOPs among companies listed in the NSE since they may be helpful in enhancing financial performance of the companies and therefore achievement of robust economic growth. It is essential to have someone in the company who knows ESOPs well and is charged with working with a qualified ESOP plan administrator.

Since the study deduced that ESOP generally affects the financial performance of the firms listed in the NSE positively, the researcher recommendation is that the management should incept and implement company policies that are in line with the interest of both employees and employers to promote full employee engagement and productivity and same time maximizing return for the firm. This can be achieved by encouraging employees to take up the ESOPs among the companies listed in the NSE and by having a high-involvement and open culture necessary for an ESOP to thrive.

Due to strong positive relationship of ESOPs and financial performance, public policy recommendation should be formulated by the Government of Kenya to promote broad based ESOP which in turn enhances national saving and facilitate as well as encouraging the development of small to medium, privately owned enterprises including startup companies.

The study also recommends that a public policy formulation encouraging investors to promote broad based ESOPs in their investments and enterprises. This is because for the entrepreneurial savvy owners who have worked for years to expand their business and in the hope of secure retirement, ESOPs allows for intermediate scale back on daily business running. Policy also should facilitate employee buyouts scheme and business succession, viable alternatives to for divestures and spin offs.

5.4 Limitations of the Study

Whilst the results from this study if interesting, there are several shortcomings that are compelling. The data collected was from similar companies listed in the NSE, thus results suffering from common method variance. In addition, data was tedious to collect and compute as it was in very raw form.

The method used in the approach gives forth to concerns regarding possibility of omitted variables. Worth of mentioning is the culture in the organization may be important factor influencing the financial performance. Further, the financial performance computations may be inconclusive. For instance, the extent of firm's foreign based operations and the structure of ownership might have impact on their financial performance. These variables were excluded due to data and cost constraints.

Further, the model may not be reliable due to some shortcoming of the regression models. Due to the shortcomings of regression models, other models can be used to explain the various relationships between the variables.

In addition, the historical background of each company was not collected yet it may be an important influence on ESOP attributes important in relationship to performance. For instance, if an ESOP bailed a company from insolvency, then the ESOP may be more out of equity principles as opposed to if the ESOP arose out of possible tax deductions savings.

5.5 Suggestions for Further Research

The paper examined the effect of ESOPs on financial performance among companies listed in the NSE in Kenya. Study recommends that a similar study to be done on other firms not listed in the NSE to allow for generalization of the effect of ESOPs on financial performance in Kenya. This is because unlisted companies have different approach to their operations not following the CMA guidelines which affect their financial performance.

The literature on ESOPs strongly suggests that devoid of employee participation, the effort geared encouraging ownership of shares by employees is likely to be fruitless. The fruitfulness of

ESOPs may also be culturally unique to a specific culture or country so research is needed to ascertain whether Kenyans have similar perceptions towards ESOPs.

Further studies should also be done on the various aspects of ESOP valuation, including the repurchase obligation and selecting an appraiser and how they affect the financial performance of the firms listed in the NSE. In addition, a study should also be done on the effect of board compensation, trustee selection and responsibilities, and employee roles on boards on financial performance of ESOP companies.

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Appendix I: Approved ESOPS at the NSE

1. East African Breweries Limited
2. Equity Bank (K) Ltd
3. Kenya Commercial Bank (K) Ltd
4. Athi River Mining Ltd
5. Access (K) group
6. Safaricom Ltd
7. Housing finance Company of Kenya
8. Scangroup Ltd

Appendix II: Number of ESOPS

(000) in units

YEAR	EABL	EQUITY	ACCESS	SCAN	SAFCOM	HFCK	KCB	ARM
2005	658,979	90,565						
2006	658,979	90,565		159,000				99,055
2007	658,979	362,210	199,885	160,000			1,996,000	99,055
2008	790,774	3,702,777	203,581	220,689	40,000,000	115,000	1,996,000	99,055
2009	790,774	3,702,777	203,581	220,689	40,000,000	115,000	2,217,778	99,055
2010	790,774	3,702,777	207,227	234,570	40,000,000	230,000	2,217,778	99,055
2011	790,774	3,702,777	208,084	284,789	40,000,000	230,000	2,217,778	99,055
2012	790,774	3,702,777	208,084	284,789	40,000,000	230,600	2,970,250	495,275
2013	790,774	3,702,777	208,084	284,789	40,000,000	230,600	2,970,250	495,275
2014	790,774	3,702,777	208,084	284,789	40,000,000	230,600	2,970,250	495,275
2015	790,774	3,702,777	208,084	284,789	40,000,000	230,600	2,970,250	495,275

Source: NSE, (2015).

Appendix III: Total Assets

TOTAL ASSETS (000)

YEAR	EABL	EQUITY	ACCESS	SCAN	SAFCOM	HFCK	KCB	ARM
2005	-	11,456,423	-	-	-	-	-	-
2006	-	20,024,000	-	-	-	-	-	42,543
2007	-	53,076,000	-	-	-	-	120,479,553	45,046
2008	-	78,879,000	2,700,845	-	-	14,294,368	191,211,584	635,247
2009	-	100,812,000	2,600,658	3,933,148	-	15,905,676	195,011,845	103,324
2010	26,736,301	143,018,000	2,728,978	8,008,431	70,671,505	23,046,540	251,356,200	140,915
2011	34,202,144	196,294,000	2,415,111	8,489,939	80,488,096	33,417,483	330,716,159	205,490
2012	32,100,534	273,170,000	2,265,745	8,646,961	122,575,845	45,113,602	368,018,785	269,531
2013	31,949,013	277,729,000	2,365,000	12,744,143	130,030,299	47,389,377	390,850,779	297,052
2014	35,405,000	344,572,000	2,459,600	13,284,104	134,600,946	60,961,680	490,338,456	369,125
2015	42,009,000	428,062,000	2,557,984	12,468,479	156,957,626	71,659,434	558,094,154	519,366

Source: NSE, (2015).

Appendix IV: Earning after TAX

EARNINGS AFTER TAX Kshs.000

YEAR	EABL	EQUITY	ACCESS	SCAN	SAFCOM	HFCK	KCB	ARM
2005	-	344,589	-	-	-	-	-	-
2006	-	754,000	-	-	-	-	-	356,000
2007	-	1,890,000	-	-	-	-	3,950,000	421,651
2008	-	3,910,000	201,984	-	-	136,427	4,191,000	503,454
2009	-	4,234,000	155,505	3,933,148	-	92,337	4,084,000	645,774
2010	8,838,000	7,132,000	(7,259)	8,008,431	15,148,038	141,796	7,178,000	792,011
2011	9,014,175	10,325,000	109,084	8,489,939	13,158,973	212,694	10,980,000	1,150,498
2012	10,823,242	12,080,000	151,377	8,646,961	12,627,607	319,041	12,203,000	1,245,638
2013	6,755,045	13,278,000	220,700	12,744,143	17,539,810	995,196	14,341,568	1,348,803
2014	6,858,000	17,151,000	286,910	13,284,104	23,017,540	975,336	16,848,862	1,493,393
2015	9,575,000	10,426,000	372,983	12,468,479	31,871,303	765,806	19,623,071	7,722,106

Appendix V: Average inflation

Inflation

YEAR	AVERAGE INFLATION
2005	7.8%
2006	6.0%
2007	4.3%
2008	15.1%
2009	10.6%
2010	4.3%
2011	14.0%
2012	9.4%
2013	5.7%
2014	6.9%
2015	6.6%

Source: Kenya National Bureau of Statistics (2015).