



CORPORATE GOVERNANCE IN AFRICA CASE STUDY SERIES: NO 10

To be or not to be executive?: A case study on corporate governance in an owner-managed company in Kenya

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PO Box 610, Bellville, 7535, South Africa.

Email: governance@usb.ac.za

www.governance.usb.ac.za

Submitted by Joyce Waiharo, email: jwaiharo@gmail.com

Abstract

This case study looks at the issue of corporate governance in Africa in an environment in which the private sector consists primarily of small and micro-entrepreneurs. With the exception of South Africa, most stock exchanges in Africa are still considered to be emerging. Enforcing corporate governance regulations necessary to encourage business owners to invest in their countries in a productive and sustainable manner and possibly attract direct foreign investment is therefore a challenge.

According to the Sample Code of Practice for corporate governance developed by the Private Initiative for Corporate Governance in Kenya, corporate governance is defined as:

the manner in which the power of a corporation is exercised in the stewardship of the corporation's total portfolio of assets and resources with the objective of maintaining and increasing shareholder value and satisfaction of other stakeholders in the context of its corporate mission.¹

Corporate governance includes ensuring that the board of directors:

has set strategic objectives and plans to put in proper management structures that will facilitate the achievement of the company's objectives and plans, and that the structures that have been put in place uphold corporate integrity and responsibility towards all stakeholders

initiates, evaluates and monitors strategic decisions and actions of management and holds them accountable is not a mere formality, leaving management to make all the strategic decisions

is responsible for ensuring the corporation operates within the mandate given to it by the shareholders and utilises its resources efficiently and effectively to meet the expectations of the shareholders.

¹ Private Sector Initiative for Corporate Governance. 1999. *Principles for Corporate Governance in Kenya and a Sample Code of Best Practice for Corporate Governance*. www.ecgi.org/codes/documents/principles_2.pdf. (Accessed 22 December 2008).

Implementation of corporate governance is difficult if there is no governance framework in place. It is also a costly process which many business owners are not really willing to invest in.

This case study illustrates the challenges corporate governance is facing in Africa.

Background to Kenstar Travel Company

Kenstar Travel Company is one of the largest travel companies in Kenya, with four branches located in the capital city of Nairobi. The company has a turnover of about R50 million per annum and 121 staff members.

Kenstar is owned by Ken Mwangi and Elizabeth Mwikali. Elizabeth currently holds a 45% share in the company and Ken holds the other 55%. Ken is the managing director and oversees the financials of the company, whereas Elizabeth is the marketing director and in every sense of the word steers the company. All employees report to her and she approves anything requiring approval. The two also comprise the board of directors of the company.

The company partnered with an experienced business travel management company, Global Travel Management. This put it on the map globally, enabling it to optimise travel programmes and to provide high quality service to clients. It also helped to optimise client savings.

Although this partnership gave Kenstar an advantage over other local travel companies, over the years, the business has grown smaller. It has lost many of its multinational and NGO clientele to competitors, and so had to close the implant offices it used to operate, only retaining its 4 core branch offices. A branch in a remote town outside Nairobi was also taken over by a competitor.

The agency started facing a cash flow problem. A number of issues contributed to this. The introduction of zero commissioning by the airlines meant that there was a decline in the revenue stream in the ticketing department. The company needed to look for additional revenue generating activities other than the sale of air tickets. Nevertheless, it decided to continue with ticket sales since Elizabeth came from a ticketing background. She also felt that ticketing was how they had grown the business.

The leisure sales department continued to do well and would have been able to sustain the company had more resources been put into it. But once the airlines cut back on their commissions, the competition became stiffer and the company began to lose a large number of corporate accounts, it also had to start cutting back on this part of its operations.

The issue of management also being the board of directors

Had Ken and Elizabeth had been answerable to a board of directors, would Kenstar have made different and possibly better decisions? Also, were Ken and Elizabeth the best people to act as managers in their company, or should they have hired competent managers to run the business? These questions and others were put to staff at Kenstar and are reported on below.

Employees commented that one of the problems in the company was that when management is also part of the board of the directors, decisions are usually made by the majority shareholder. No one else has a say. Sometimes these decisions were made on an emotional basis. Some employees felt that if decisions made as a team of top management, they would be more rational and objective.

Employees also commented that the majority shareholder micromanages every aspect of the business, being responsible for the hiring of staff and salaries, and at times even doing the work of the travel consultant. This comprehensive set of duties and involvement in the minutiae of the business begs the question of when management has time to handle their own duties, let alone think strategically as a member of the board.

Interviewees said that management is unwilling to let go of the company they formed and the way they have always run their business and implement new strategies. As an example, staff gave the occasion when the company invited consultants to hold a seminar on how to boost productivity. Management also participated in the seminar. The consultants made their recommendations and solutions but to date, nothing has been implemented. This was frustrating for employees who felt that these recommendations would have improved their working environment, especially as the solutions had emerged from their feedback.

Interviewees also mentioned hastily made decisions resulting in last minute changes by management as a source of frustration. In many instances, projects that were ready to start were abruptly stopped, resulting in a waste of resources.

Fear of being reprimanded or losing their job meant that appointed managers felt they were not in a position to redirect the directors/shareholders. Even if they held a different point of view, they aligned themselves to the owners' way of thinking or decisions.

Staff felt that management's omnipotence meant that there were no checks to 'bring them down to ground level', or even to discuss ideas that could be of use to the business. They say that the directors feel they have worked so hard to get the company to where it is that they are not willing to take a backseat, but the danger in this is that when the business starts growing it gets too much for one person to keep tabs on what is happening. Key issues that brought the business growth, such as personalised customer service, are then neglected. This is one of the reasons that Kenstar ended up losing clients: they were not aware of exactly who their client base was and were not providing 'top-notch' service. Neglected clients were snapped up by other small up-and-coming competitors.

Another comment was that with the growth of the business, management did not assign more resources to new business, but made use of existing resources. For instance, a tour consultant comfortable with handling 10 corporate clients now had to service 20. The tour consultant would be unlikely to be able to provide the personalised service they were previously known for. They are more prone to errors as they are under pressure. They also end up working much longer hours and are not 'at their best'. The result is conflict with clients.

In a bid to keep costs low, the owners have also neglected the wellbeing of their employees, resulting in a high turnover, which is detrimental to the company as this is a very service oriented business. Clients are not pleased with being handled by different staff members. One of the major reasons for the high turnover is that the employees feel that they are not duly compensated. The other reason is a rigid work environment, which stifles creativity. Employees are told to follow the prescribed manner that the owners have used for years. In essence, entrepreneurialism is not encouraged.

Regarding corporate governance, some employees felt that these principles could not be administered by the travel and tour associations, as a company can choose which association to subscribe to and does not have to implement the rules. Adhering to corporate governance principles would mean being transparent. Many smaller organisations want to keep the secrets of their success to themselves and do not want to divulge their financial records. Only the owners know how the business is performing.

In short, staff at Kenstar felt that change was not imminent as long as the business is profitable.

Possible solutions and ways to implement corporate governance

In Africa we are faced with the challenge of most corporations being family-owned, small private companies or community-based initiatives such as co-operatives. As a result, the regulatory and supervisory systems are generally weak, which contributes to the grey area of corporate governance within these corporations.

Most of these companies do not see the values of instilling corporate governance within their operations as this may have financial implications. They also see nothing wrong with the way they have been operating for years. After all, they argue, they are still in business. However, they could have progressed much further with the guidance that corporate governance provides.

The majority shareholders in these corporations end up being the same members on the board of directors and acting as the management of the very same company. They are not able to abide by the corporate governance rules and tend to be caught in situations where they are wearing two hats at the same time. This is particularly confusing to employees and hampers the growth of the company.

To resolve this dilemma, it seems obvious that companies should simply appoint an external board of directors or step away from their executive management roles and hire competent managers. However, they are so intricately involved in these businesses that it is not so easy to let go. So how is corporate governance to be implemented in these institutions?

One suggestion is to award shares to the employees as an incentive. It would also introduce a forum where the board of directors can have a neutral perspective geared to the betterment of the company. This could be a start in implementing corporate governance, but that is not likely to happen in many small and medium-sized firms in the near future, barring a miracle.

Corporate governance education seminars would be one way of addressing this issue. Several types of organisation could be invited and could apply their current experience to the case studies at hand.

Companies can also decide to go back to the drawing board and develop goals, mission statements and objectives which could be a starting point for the corporate governance framework. Most of these companies have no clear policies or long-term planning, and this could help steer them in the right direction. It could also help alleviate the danger of power abuse as the dual roles of both owners and shareholders do not have any checks and balances to control them.

A succession plan is essential. Should anything happen to the owners, it could mean outright closure for the company since the owners hold all the information, so for business to continue as normal would take time and operations may have stalled by then.

To be able to bring about any form of corporate governance, the delegation of duties is one aspect that has to be instilled in these companies. Delegating means empowering all employees to do what has been assigned to them. The chain of command should be clear and unambiguous, enabling senior management to handle their work processes in the most efficient way possible. It should also be made clear that in any organisation, the role of the board of directors is to provide strategic direction to the company.

Corporate governance in Africa is still in its infancy and has many challenges it needs to overcome but we are headed in the right direction once we tackle the issue at hand: 'to be or not to be executive?'