INSTITUTE OF DIRECTORS
SOUTHERN AFRICA

African Governance Showcase 2017

From a desk to the board room:

How Equity Bank morphed into
A regional stallion jockeyed by good governance

IFC International Finance Corporation
WORLD BANK GROUP

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Problem statement

Over the years, bad corporate governance practices by Boards of directors have caused many financial institutions to stagnate and collapse. Similarly, Equity faced serious underperformance in its first years which necessitated a turnaround strategy by the Board in order to help the company out of financial failure. This case study demonstrates how applying good corporate governance practices within a professionally run board of directors led to the growth of a bank from a small failing financial entity to a regional banking giant in Africa.

Background

In 1984, Kangema was a small but bustling town in what was then Murang'a District in Kenya's Central Province. Surrounded by smallholder farms growing tea, coffee and subsistence crops Dr. Peter Munga founded Equity Building Society, ostensibly to provide mortgage financing for the majority of customers who fell into the low income population. Together with four other friends, the gentlemen became involved in management and administration of the young institution, driven by the opportunities of creating a homegrown financial institution within a difficult socio-economic environment.

Poor management and insufficient supervision by the board of directors, among other factors, contributed to its deterioration and a decade after its inception, the Central Bank of Kenya (CBK) warned that Equity was on the verge of insolvency.[1] It was losing KShs.5 million (approximately USD60,000 then) annually, non-performing loans were 54% of the portfolio, and accumulated losses totaled KSh.33 million (USD500,000), on a paid up capital of KShs.3 million. Equity's liquidity ratio stood at 5.8%, far below the regulatory requirement of at least 20%.[2] Kangema's flame of financial independence was about to be extinguished by technical insolvency.

The roots of the need for governance 1994-2004

In 1994, with the sword of insolvency dangling over their heads, it had become sharply apparent to the building society's board of directors that it was about time to include independent members in their rank and to recruit externally for managers.[3] This was an easy decision to make on paper but a difficult one to expeditiously execute. Equity gradually strengthened its Board, and by the year 2000, four new members were introduced,[4] including the dynamic Finance and Strategy Director Dr. James Mwangi who was instrumental in the turnaround of the bank's health. The fact that it took up to six years to bring in four new members is illustrative of the mind set shift that was required to let in "outsiders" into the fairly insular board dynamic at the time. But once the governance horse had bolted, there was no turning back and a key resulting milestone was the conversion of the organization from a less regulated building society into a fully-fledged commercial bank on 31st December 2004.

Now that the institution was under the even stricter commercial banking purview of the Central Bank the board set about establishing its own Code of Corporate Governance together with the attendant board charters and committee terms of reference which were internally designed comprehensively in 2005 with external professional assistance.

Formation of the first equity bank board ± 2005

The Board was constituted with eleven directors, led by the founder Dr. Peter Munga, as non-executive Chairman. Dr. James Mwangi, who is now the Chief Executive Officer and Managing Director, was appointed as the only Executive Director. Sevennon-executive directors were appointed, including two females, recruited primarily for their good mix of skills, experience and competencies in various relevant fields of expertise rather than shareholding. Finally, two directors were appointed to the board to represent Africap ± an institutional investor. This was a notable difference from the previous insular board as it now reflected gender and national diversity that would inject fresh strategic thinking and fiduciary oversight on the organization driven by the combined management and governance experience of the directors.

It was on this basis that seven board committees were constituted as follows:

- Audit
- Risk Management
- Credit
- Systems and Processes
- Strategy and Investment
- Governance, Board Nomination and Staff Remuneration
- Tendering and Procurement.

It is notable that "systems and processes" warranted the full-time attention of the board through a committee and is demonstrative of the new board's determination to move into the commercial banking realm. This committee later fell away by 2007 as the bank's systems became mainstream.

Decision making in the first year of Equity Bank's operations then moved from the individualized culture of the building society's management to a more collaborative and accountable structure that the board committees established. The committees' role was to provide overall strategic direction, review performance, take material policy decisions and ensure that the Bank met its responsibilities to its shareholders and other stakeholders. [5] Each of the directors subscribed to the Code of Corporate Practices that set out their duties and responsibilities. The Code also provided for the evaluation of board members' performance bi-annually.

The Board also passed a resolution barring non-executive director from obtaining loans, guarantees and other credit facilities from the Bank during their tenure of office even though the Banking Act of Kenya allowed Directors to obtain a facility or advances from a Bank.

In addition, the memorandum and articles of association were amended, barring directors and their associates from trading with the Bank. [6] These resolutions were made to avoid conflicts of interest within the Board. The bottom line results in the first year of bank operations demonstrated not only the management's strength, but also the benefits of the stronger strategic and accountability mechanisms that had been embedded by the Bank's board. The Bank reported a profit before tax of KShs.500.5 Million (USD4.8m today) in 2005 compared to the KShs.218.3 Million (USD 2.1M) that it had reported in its previous year of existence as a building society, an impressive growth of 128%.

From a bank to a group 2006 - 2014

On 7th August 2006, the Bank undertook a listing at the NSE. The listing also attracted Helios, a strategic investor supported by IFC, CDC and OPIC, to invest USD 185 million in 2007.This led to the entry of two new Helios appointed directors on the board to continue adding the aggressive growth focus that the board had inculcated in the firm. There was also a notable shift in the board make up with three non-executive directors dropping off to make room for the Helios directors.

The Equity boardroom now had a new level of international perspective, having come a long way from its origins on the slopes of the Aberdare range in Murang'a district. It also ensured that the disclosure standards for the bank's operations and performance would be benchmarked at a higher level and would be open to scrutiny from both local and international investors.

The Bank continued to grow and set up subsidiaries in Uganda, South Sudan, Rwanda, Tanzania and most recently the Democratic Republic of Congo. Their shares were also listed on the Rwandan and the Ugandan Stock Exchanges. A key plank of this expansion was the appointment of local directors in all the subsidiaries. Having learnt from their Kenyan experience, the presence of local knowledge and context on the subsidiary boards continues to be a critical pillar to the success of the subsidiaries. The Board it established a framework of rules, relationships and principles that were applicable throughout its entire organization to enable it succeed and deliver long-term and sustainable value. In line with this, the subsidiaries implemented their own codes of corporate governance as well as Board charters and committee charters which are benchmarked by the Group Board governance standards.

At the end of 2014, the Group undertook a restructuring by creating a non-operating holding company. This was one among the governance practices by the Board to safeguard the risk of the subsidiaries as well as to benchmark against international best practice. The Group changed its name to Equity Group Holdings Limited and now operates as a non-operating holding company licensed by the CBK with six regional banking subsidiaries and other non-banking subsidiaries including its investment bank and telecoms subsidiary Finserve Africa. As at the end of the 2016 financial year, the Equity Group Board had four foreign directors out of its nine directors providing global perspectives to a regional bank. All these fairly complex changes have required the board to set up global best practice standards with regards to board processes.

Current Board processes

The Group Board has a Board Governance and Nominations Committee (BGNC) responsible for all aspects of appointment of the Bank's Group and subsidiary directors. The Board has ensured that there is proper succession planning, and that processes and plans are in place with regard to both Board and Senior Management appointments. Board directors have also continuously had access to continuous professional development courses to enable them to maintain and deepen their knowledge and skills and to fulfill their responsibilities as Directors.

Furthermore, the Group Board has established four Board committees to assist in guiding the direction of the bank. These are the Audit, Risk Management & ALCO, Governance, Nominations and Staff Remuneration, as well as Strategy & Investment Committee. All the committees are governed by charters setting out their mandates and authority as well as clear terms of reference. The Board reviews the effectiveness and performance of the committees annually and reviews the mandates of the committees periodically to ensure that they remain relevant.

Additionally, the Board has put in place a formal process for reviewing its performance and that of its Committees and individual Directors through an evaluation undertaken by and independent evaluator. Upon completion of the exercise, all the Board members discuss the Board evaluation results and create an action plan to address outstanding matters that may have arisen is produced for immediate execution and tracked on the board's agenda.

Conclusion: Good governance results in growth

In part largely due to good corporate governance within the Board, Equity has gone through exponential growth in its 13 or so years of existence as a commercial banking entity. This has enhanced investor confidence at both a local and international level thereby increasing the share capital of the Group.

Equity Group Holdings Limited currently has more than 11 million customers making it one of the largest in terms of customer base in Africa. [7] Its balance sheet has grown 41 times from KShs. 11.4 billion (USD 110M) in its first year of business to KShs 473 billion (USD 4.6 billion) thirteen years later in 2016.

Equity Bank has also received accolades including the Best Retail Bank in Africa 2017 in the African Banker Awards. It is also ranked among the Top 1000 Banks in the World. It has been ranked 2nd in Kenya, 21st in Africa and number 806 in the world. [8] By regularly publishing its corporate governance framework in its annual accounts for the scrutiny of investors and analysts alike, the Bank and Group Board have consistently set a very high standard of accountability that has attracted both local and foreign institutional investors who typically place a premium on governance. From the wind swept dusty roads of Kangema to Nairobi's Upperhill financial district, Equity Bank has proved that unrelenting focus on growth overseen by a largely independent and highly professional board can change the fortunes of an institution.

Discussion questions for reflection

1. Discuss the good corporate governance practices that have been applied within the Equity Board throughout the years and their bearing on the strategy of the organization.
2. What are the characteristics of an effective Board of Directors? Evaluate the effectiveness of the Board of Equity during its different stages of growth.
3. How has the expansion of Equity from a small building society into a regional affected the board structure and board processes of Equity?
4. In your opinion, are there any more aspects of good corporate governance practices that the board can apply to improve the corporate governance at Equity?

1. BBC News, Kenyan hopes to open up banking to the poor, 12 December 2011, retrieved from http://www.bbc.com/news/world-africa-16109757 accessed on 30th August 2017

2. Graham A.N. Wright and David Cracknell, The Market Led Revolution of Equity Bank, MicroSave Briefing Note # 63 retrieved from http://www.microsave.net/files/pdf/BN_63_The_Market_Led_Revolution_of_Equity_Bank.pdf accessed on 30th August 2017

3. Kenyan hopes to open up banking to the poor, 12 December 2011, BBC News retrieved from http://www.bbc.com/news/world-africa-16109757 accessed on 30th August 2017

4. Graham A.N. Wright and David Cracknell, The Market Led Revolution of Equity Bank, MicroSave Briefing Note#63retrievedfromhttp://www.microsave.net/files/pdf/BN_63_The_Market_Led_Revolution_of_Equity_Bank.pdf Accessed on 30th August 2017

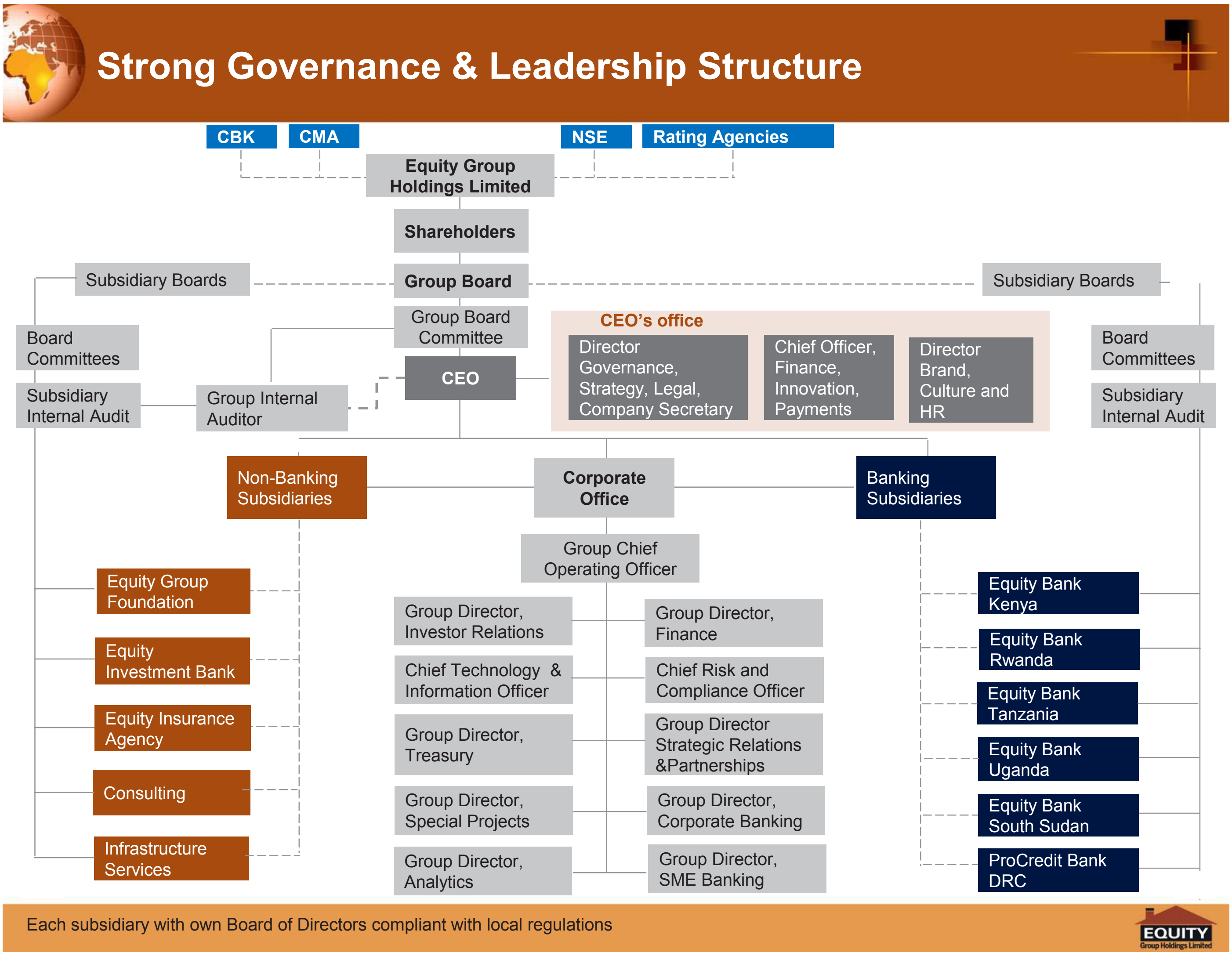
5. Equity Bank Annual Report ± 2005

6. Statement on Corporate Governance, Equity Bank Annual Report 2005

7. History of Equity Bank, Equity Bank Group Website retrieved from http://equitybankgroup.com/about/our-history accessed on 31st August 2017

8. Bankers Magazine, retrieved from http://www.thebanker.com/Top-1000 accessed on 31st August 2017

Appendix 1


Strong Governance & Leadership Structure
CBK
CMA
NSE
Rating Agencies
Equity Group Holdings Limited
Shareholders
Subsidiary Boards
Group Board
Subsidiary Boards
Board Committees
Group Board Committee
CEO's office
Board Committees
Subsidiary Internal Audit
Group Internal Auditor
CEO
Director Governance, Strategy, Legal, Company Secretary
Chief Officer, Finance, Innovation, Payments
Director Brand, Culture and HR
Subsidiary Internal Audit
Non-Banking Subsidiaries
Corporate Office
Banking Subsidiaries
Group Chief Operating Officer
Equity Group Foundation
Equity Investment Bank
Equity Insurance Agency
Consulting
Infrastructure Services
Group Director, Investor Relations
Chief Technology & Information Officer
Group Director, Treasury
Group Director, Special Projects
Group Director, Analytics
Group Director, Finance
Chief Risk and Compliance Officer
Group Director Strategic Relations &Partnerships
Group Director, Corporate Banking
Group Director, SME Banking
Equity Bank Kenya
Equity Bank Rwanda
Equity Bank Tanzania
Equity Bank Uganda
Equity Bank South Sudan
ProCredit Bank DRC
Each subsidiary with own Board of Directors compliant with local regulations
EQUITY
Group Holdings Limited

Appendix 2 - Equity Group Holdings Limited Corporate Governance Parameters

EQUITY GROUP HOLDINGS LIMITED CORPORATE GOVERNANCE PARAMETERS

CORPORATE GOVERNANCE PARAMETERS	**RESPONSE/ REMARKS**	**ENFORCEMENT POLICY/CODE/ARTICLES**
STRUCTURE OF THE BOARD		
Age diversity	Average age is 60 years	
Academic qualifications	In line with the Group's pursuit of recruiting highly competent individuals, all Board members have professional and academic qualifications; most being holders of Masters Degrees and others PHD holders.The professional qualification ranges from accounting to Human resource.	Code of Corporate Governance
Professional experience	Thirty Five (35) years	
Professional diversity	Board members have expertise in the following fields: accounting, financial management, banking, leadership and management, information and communication technology, applied mathematics, environment and conservation, strategic planning, business development and growth, operations, project management, auditing, business administration, investments, privatisation in emerging markets and human resource.	Code of Corporate Governance
Gender ratio of Female: Male of board members	the ratio is 2:7	
BOARD OPERATIONS AND CONTROLS		
Appointments of Board Members	The Board ensures that there is a formal and transparent procedure in the appointment of Directors to the Board and all persons offering themselves for appointment, as Directors should disclose any potential area of conflict that may undermine their position or service as Director. The Board considers academic qualifications, technical expertise, experience, age and gender. The new directors are presented to the Central Bank of Kenya for approval and also submitted to the shareholders in an Annual General Meeting for approval. Further, there is established the Board Governance, Nominations and Compensation Committee, which is tasked with, among other duties: a) regularly reviewing the required mix of skills and experience in order to assess the effectiveness of the Board and making recommendations to the Board for new appointments and other changes to the Board; b) ensuring that the Chief Executive Officer promptly submits to the CBK an annual report on Board and directors evaluations and effectiveness; and c) Periodically reviewing the completeness and effectiveness of all corporate governance policies and initiatives, including the Code. At a minimum, there are always at least 3 members of the Board Governance, Nominations and Compensation Committee, the majority of whom are Independent Non-Executive Directors. **Procedure of Appointment** 1. **Shareholders** are ultimately responsible for appointments to the Board subject to approval from Central Bank of Kenya. 2. Information shall be availed to Shareholders, 21 days in advance of any decision making so that Shareholders ensure that only credible persons who can add value to the Group are elected to the Board. 3. Board members appointed shall receive formal letters of appointment setting out the main terms and conditions relative to their appointment. 4. Appointments to the Board is made through an organized and effective process that ensures the appointment of a diverse and balanced mix of proficient individuals. Appointments to the Board consider academic qualifications, technical expertise, experience, nationality, age and gender. The Board establishes and appoints chairpersons to relevant committees and delegate specific mandates to such committees as may be necessary including internal audit, risk management, remuneration, Board nominations, finance, investments and governance.	The Memorandum and Articles of Association, Code of Corporate Governance.
induction framework for new Board members	On appointment to the Board and to Board committees, all Directors receive a comprehensive induction on their individual requirements (where applicable) in order to become as effective as possible in their role within the shortest practicable time. In accordance with the Group Code, new Directors undergo induction with the objective of: a) building an understanding of the nature of the Group, its business and the markets in which it operates; b) building a link with the Group's staff; c) building an understanding of the Group's main relationships; and d) Ensuring an understanding of the role of a Director and the framework within which the Board operates.	Code of Corporate Governance

CORPORATE GOVERNANCE PARAMETERS	RESPONSE/ REMARKS	ENFORCEMENT POLICY/CODE/ARTICLES
STRUCTURE OF THE BOARD		
	These skills and knowledge shall be updated at regular intervals. The induction is designed by the Company Secretary in consultation with the Chairperson and will include meetings with Directors, Senior Management and key external advisors to assist the Directors in building an understanding of the Group's operations, the key risks it faces and the Group's risk management policy.	
continuous skills development program	Board members have access to continuous professional development courses on relevant issues and additional business awareness sessions to enable them to maintain and deepen their knowledge and skills and to fulfil their responsibilities as Directors. Directors are provided with regular updates on matters relevant to legal reforms, corporate governance, the corporate environment, regulatory obligations, business/commercial risks and other matters that may be of interest in the execution of their role. The Board ensures that training is provided to enable members to increase their competency and expertise. The Chairperson regularly reviews and agrees with each Board member on his or her development needs. The Board allocates sufficient time, budget and other resources for this purpose. In 2016 the training programs provided to directors were as follows: i. Navigating the sea of change: How to stay afloat; ii. Strathmore Business School: The Effective Director; iii. New Companies Act: Role of Directors; and iv. New directors underwent extensive induction.	The Code of Corporate Governance
Performance- Annual performance evaluation of Board members	Board evaluation was conducted by an independent consultant, whereby evaluation was performed on the Chairman of the Board, Board members, including the CEO, Board committees and the Company Secretary, by means of one on one interviews, as well as questionnaires. The Board evaluation questionnaire focused on the following key areas: i. Board Structure; ii. Board Composition; iii. Board Role and Responsibilities; iv. Key Board Functions and Processes; v. Board Information; vi. Board Meetings; vii. Board Relationships;	The Code of Corporate Governance
	viii. Board Development; and ix. Overall Performance and Contribution. The resultant reports are filed with the regulators as required.	
Policies and procedures for remunerating the board of directors	The Board determines the remuneration of Directors, subject to Shareholder's approval. Directors' remuneration is sufficient to attract and retain Directors to run the Group effectively and is competitively structured and linked to performance, but is also balanced against the need to ensure that the Group's funds are not used to subsidise an excessive remuneration package. Non-Executive Directors do not receive any salary. Particulars of compensation of directors and key personnel are disclosed to the public in the audited financial statements.	The Code of Corporate Governance
Board Charter	The Board Committees reviews the charter at least annually and update it as needed to respond to changing oversight needs.	The Code of Corporate Governance and Memorandum and Articles of Association
Code of Ethics	The Group has adopted rules to ensure that its business is conducted according to the highest ethical standards, and in compliance with all applicable laws and regulations governing the banking industry in the jurisdictions within which it operates. These rules apply to all Directors and the Board ensures that all the Directors and Senior Management adhere to these rules, through Code of ethics and conduct policy ,Conflict of interest policy, Insider trading and market abuse policy and Corporate reporting and accountability policy The Group has a zero tolerance policy for all forms of corruption, bribery, fraudulent conduct and unethical business practice. The Group is fully compliant with the Bribery Act, Proceeds of Crime and Anti-Money Laundering Act and the Anti-Money Laundering Policy of the Group. Additionally, the Group is fully compliant with the Prevention of Terrorism Act.	The Code of Corporate, Governance Code of ethics and conduct policy ,Conflict of interest policy, Insider trading and market abuse policy and Corporate reporting and accountability policy
Board meetings in a year (in 2016)	At a minimum, Board meetings are held Quarterly. In 2016, there were 5 meetings, held in February, March, April, July and October.	The Code of Corporate Governance
Removal or exit of existing board directors	Every year at least one third of directors retire by rotation and are subject to election by shareholders if desired to continue in office.	The Memorandum and Articles of Association and Code of Corporate

CORPORATE GOVERNANCE PARAMETERS	RESPONSE/ REMARKS	ENFORCEMENT POLICY/CODE/ARTICLES
STRUCTURE OF THE BOARD		
	The Board may remove a Director by ordinary resolution. The Board ensures that the CBK, NSE and CMA is informed of the resignation and/or removal of any Directors or the Chairperson within 7 days of the time such person vacates that office.	Governance
Is there a term limit for the board of directors?	In accordance with the Code, the tenure of an Independent Board member is a cumulative term of 9 years, after which the Board member is re-designated as a Non-Independent member. Also, upon the attainment of 70 years, directors resign from office at the following annual general meeting and can only continue serving as directors upon obtaining the approval of the shareholders at the Annual General Meeting.	The Memorandum and Articles of Association and Code of Corporate Governance

A. PRINCIPLES OF CORPORATE GOVERNANCE

The Group adheres to the following principles of corporate governance

a. Principle on Appointment, composition, size and qualifications of Board members;
b. Principle on Board composition;
c. Principle on structure of the Board;
d. Principle on the functions of the Board;
e. Principle on Roles of Chairperson and Chief Executive Officer;
f. Principle on Tenure of Independent Board members;
g. Principle on Age Limit for Board members;
h. Principle on Induction and continuous skills development;
i. Principle on Insider Lending;
j. Principle on Board Tools;
k. Principle on Governance and Legal Audit; and
l. Principle on Insider Dealings/ Trading.

B. INDEPENDENCE OF THE BOARD

The Board ensures that no one person or group of persons shall have unfettered power and that there is an appropriate balance of power on the Board, at least three fifths of the Board are Non-Executive members and one third are Independent members so that the Board can exercise objective and independent judgment.

C. TRANSPARENCY & DISCLOSURE

The Group ensures that it facilitates public disclosure of reliable and timely information in its website and the Annual Report to enable users of that information to make an accurate assessment of the Group's financial condition and performance, business activities and risk profile. However, disclosure alone does not necessarily result in transparency. To achieve transparency, the Group provides timely, accurate, relevant and sufficient disclosures of qualitative and quantitative information that enables the public make a proper assessment of the Group's activities and risk profile.
At a minimum, the following broad categories of information is disclosed in clear terms and appropriate detail to help achieve a satisfactory level of transparency in relation to the Group. These are:

a. financial performance;
b. financial position (including capital, solvency and liquidity);
c. risk management strategies and practices;
d. risk exposures (including credit risk, market risk, liquidity risk, and operational, legal and other risks);
e. aggregate exposure to related parties and transactions with related parties;
f. accounting policies; and
g. basic business, management and corporate governance information.

D. COMPLIANCE WITH REGULATIONS AND STANDARDS

The Group performs an Internal Capital Adequacy Assessment Process and the Group ICAAP framework is reviewed annually. Further, the Group complies with the Bribery Act, Anti-Money Laundering Act and Prevention of Terrorism Act. as well as international regulations such as the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act 2001, Financial Action Task Force (FATF) Recommendations and Foreign Account Tax Compliance Act (FATCA).

E. CORPORATE GOVERNANCE POLICIES

The Group has engrained the principles of effective corporate governance in its Values and Policies, the following are some of the policies;

A. Code of ethics and conduct policy

B. Speak up policy

C. Conflict of interest policy

D. Insider trading and market abuse policy

E. Corporate governance, viability and sustainability policy

F. Corporate reporting and accountability policy

Disclaimer:

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