



## **ASSESSING SHAREHOLDER ACTIVISM AMONG RURAL BANKS: A STUDY OF BONGO AND NAARA RURAL BANKS IN THE UPPER EAST REGION, GHANA**

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### **ABSTRACT**

The question that agitated the mind of this author culminating in this study was the possibility of shareholders of rural banks holding directors of their banks accountable when appropriately empowered to do so. The core objective was to establish how shareholders are using the powers they possess to influence decision making among their banks. Adopting the qualitative research design, a self administered questionnaire was used to solicit the views of the directors and some shareholders of the Bongo and Naara Rural Banks in the Upper East Region. Various statistical models were run to establish relationships among variables. The outcome of the analysis indicated that there is a weak relationship between shareholder empowerment and shareholder activism among rural banks. Shareholders who are even aware of such powers are reluctant to use them when they feel the directors are not complying with some corporate governance practices. In view of these findings, the following recommendations were deemed appropriate and worth pursuing so as to improve upon the corporate governance practices of Rural Banks. These include ensuring that shareholders of Rural Banks are fully empowered; consciously educated on the power they possess at the point of purchasing shares; shareholder committees are set up to act on behalf of shareholders; and young people are encouraged to purchase shares of Rural Banks.

**Key Words:** Rural Banks, Shareholder Empowerment, Shareholder Activism.

### **INTRODUCTION**

There are over 540 rural banks in Ghana (ARB Apex Bank, 2012). Rural and Community Banks are unit banks owned by members of the rural community through purchase of shares and are licensed to provide financial intermediation in the rural areas. Rural Banks (RBs) were first initiated in 1976 to expand savings mobilization and credit services in rural areas not served by commercial and development banks. These banks are set up to ensure that rural communities in Ghana have access to banking facilities and a source of micro-financing for rural enterprises development.

Usually, the commercial banks are reluctant to lend to the rural communities because of the risk and cost. Rural Banks, therefore, represent the only hope of the rural community that they will have access to any financing whatsoever. In this respect, rural banks are essential to fighting poverty, rural-urban drift, and social vices in Ghana.

The Bank of Ghana is the main regulatory body of rural banks in Ghana. ARB Apex Bank is the oversight body of these rural banks but has no statutory authority; it influences its members through persuasion and training seminars. The initial capitalization of Rural Banks is through the sale of shares. The shareholders therefore, are the true owners who manage the Rural Banks through the board of directors. These directors need to be held accountable by their principal (the shareholders) so the gap between ownership and control can be minimized. Shareholders who take a keen interest in how their funds are managed are known as activists. The most common definition of a shareholder activist is an investor who tries to change the status quo through the option of “voice” without initiating a change in control of the firm (Gillan & Starks, 1998). The potential for shareholder activism arises whenever shareholders – erroneously or not – believe that the board of directors fails in their duty. That is, the shareholders are

dissatisfied with the performance of the board and presumably the performance of the firm. The Securities and Exchange Commission (SEC) of Ghana points out that, controlling shareholders who may be individuals, family holdings, bloc alliances, or other corporations acting through a holding company or cross shareholdings, can significantly influence corporate behavior. In the same vein institutional investors are in a position to demand acceptable standards of corporate governance in the companies they invest in. An activist shareholder uses an equity stake in a corporation to put public pressure on its management. The goals of activist shareholders range from financial (increase of shareholder value through changes in corporate policy, financing structure, cost cutting, etc.) to non-financial (disinvestment from particular countries, adoption of environmentally friendly policies, etc.).

The attraction of shareholder activism lies in its comparative cheapness; a fairly small stake (less than 10% of outstanding shares) may be enough to launch a successful campaign. Shareholder activism has gained popularity as management compensation at publicly traded companies and cash balances on corporate balance sheets have risen. Shareholder activism can take any of several forms: proxy battles, publicity campaigns, shareholder resolutions, litigation, and negotiations with management.

There is little or no shareholder activism among rural banks and less rigorous external regulation in relation to corporate governance (Oppong, 1990), though best practices in corporate governance suggest that shareholders and regulatory bodies play important roles to ensure adherence to governance procedures. The focus of the researcher is to establish how much power shareholders of rural banks possess to influence corporate governance, and how they are using such power to their benefit.

## **MATERIALS AND METHODS**

### **Research Design**

For a study which is centered on the various interests and activities of diverse groups of people, it is appropriate to use a descriptive survey. A descriptive survey was selected because it provides an accurate portrayal or account of the characteristics of the population; for example, behavior, opinions, abilities, beliefs, and knowledge of a particular situation, or group.

### **Sampling and Data Collection**

The target population in this research was the shareholders of Rural Banks in the Upper East Region of Ghana. There are five Rural Banks in the Upper East Region. They include; the Naara Rural Bank, Bongo Rural Bank, Builsa Community Bank, Toendi Rural Bank, and Bessfa Rural Bank Ltd. Out of these, the Naara Rural Bank and the Bongo Rural Bank were randomly selected. The characteristics of the shareholders of these banks reflect those of the other rural banks in the Upper East Region.

This research largely employed the simple random sampling technique in selecting a representative sample to represent the shareholders of each bank. However, since the shareholders are sparse, a snowball technique was used to compliment the random sampling. Snowball sampling (referral sampling) is a non-probability sampling technique where existing study subjects recruit future subjects from among their acquaintances. As the sample builds up, enough data is gathered to be useful for research. This sampling technique is often used in hidden populations which are difficult for researchers to access. In the case of shareholders, they each had a fair knowledge of where to locate other shareholders, hence a snowballing technique worked effectively.

A sample of 40 shareholders of each bank was taken, making a total of 80 respondents. These respondents were all individual shareholders. This is because they tend to be vulnerable and their interests may not be protected by the institutional shareholders. The management was interviewed to get their side of the issues concerning shareholder empowerment and how active the shareholders were. The managing directors answered the questions on behalf of management. A self-developed questionnaire was used to solicit information from the sampled shareholders. A test was conducted to ensure the validity of the questionnaire the researcher developed. For content validity, the researcher contacted some experienced researchers and experts to evaluate the constructs that were measured, and their ideas were inculcated. A face validity test was also conducted using ten shareholders of rural banks to ensure questions are well understood and unambiguous.

**RESULTS AND DISCUSSIONS**

**Shareholder Empowerment**

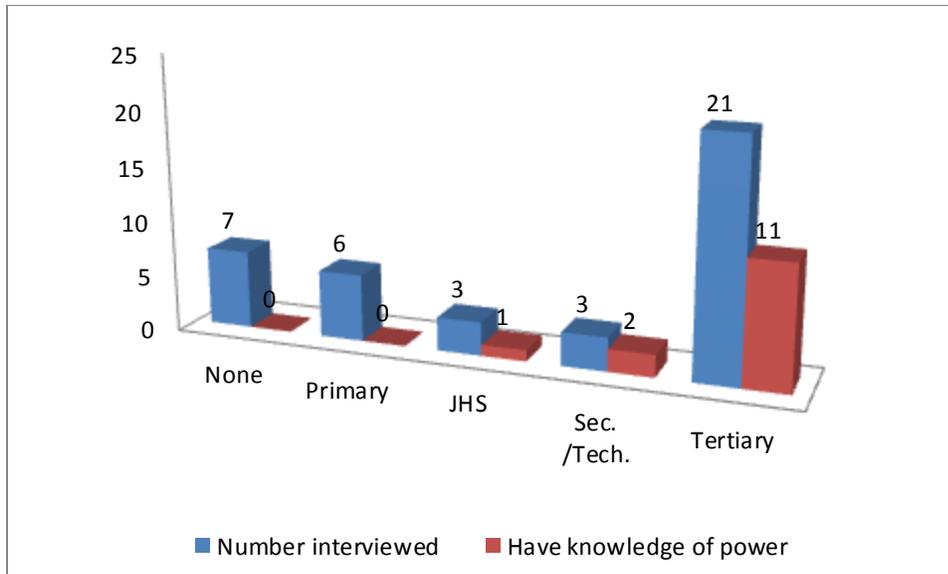
Indeed, efforts to strengthen shareholders’ power (Bebchuk, 2005) at the expense of management have become more potent in the wake of Enron, WorldCom, Parmalat and other corporate failures in various countries. The researcher first sought to find out how insulated (cut-off) the directors of rural banks are from shareholder intervention by employing and adapting the Management Insulation Index (MII) developed by Ferreira, Kershaw, Kirshmaier, and Schuster (2012). This theory sets out factors that determine the amount of power shareholders of an entity have viz-a-viz the board of directors. These factors include whether the board is classified or not, whether there are any restrictions on director nomination, and whether shareholders have the power to: appoint and remove directors, call a special meeting, and gain control over the board by increasing board size. A test of this theory in both banks show that the boards are not classified, (directors have a limit to the number of years they can serve). Shareholders have the power to: appoint and remove directors, and gain control over the board by increasing board size. At the Bongo Rural Bank, shareholders have the right to call a special meeting, while those of the Naara Rural Bank cannot do so. At both banks, there are some restrictions on director nomination by shareholders (see Table 1). Restrictions on director nomination mean that there are conditions that apply when shareholders are exercising their power of nominating directors. From the foregoing discussion, it is clear that, despite the existence of a few restrictions, the management of both banks are not much insulated from shareholder intervention.

**Table 1. Results of Management Insulation Index**

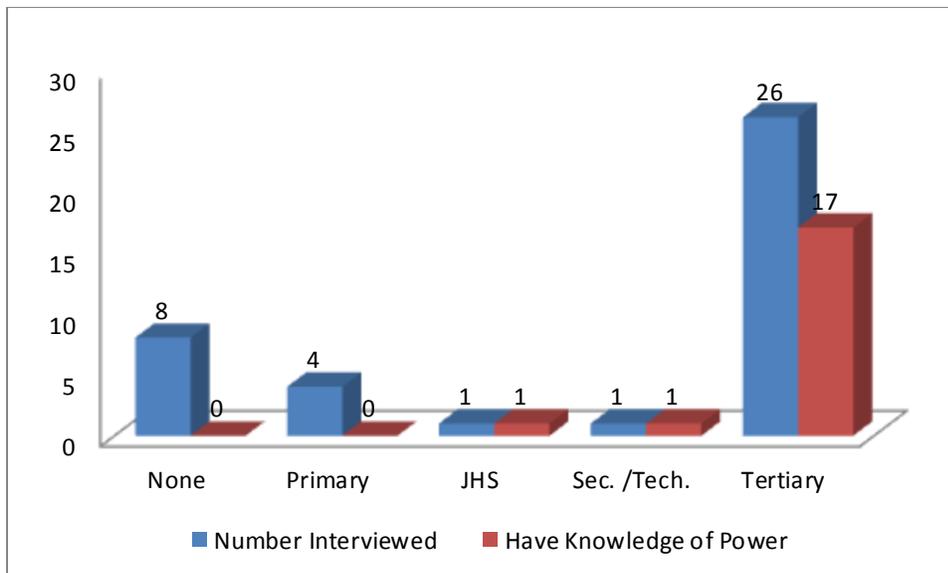
|   | Management Insulation Factor   | Bongo Rural Bank | Naara Rural Bank |
|---|--|------------------|------------------|
| 1 | Is the Board Classified?   | No               | No               |
| 2 | Can shareholders appoint and remove directors?                             | Yes              | Yes              |
| 3 | Can shareholders call a special meeting?                                   | Yes              | No               |
| 4 | Can shareholders gain control over the board by increasing the board size? | Yes              | Yes              |
| 5 | Are there any restrictions on director nominations?                        | No               | No               |

**Knowledge of Shareholder Power**

The level of knowledge of shareholder power was measured based on questions that were posed on whether the shareholders were aware of the kind of powers they possess. They were required to mention those powers they were aware of, and how they became aware of such powers. The researcher then used the responses to those questions to gauge the level of awareness they each had. The results showed that those who had gone up to the tertiary institutions had a high level of awareness (see figures 1 and 2). This is possibly because, as it came out from responses to the questions, they take it upon themselves to read from other sources such as the company’s code, Act 179 (1963) and other documents from where they gained the knowledge. These shareholders are also largely young people between ages 25 and 44 years.



**Figure 1. Relationship between Level of Education and Knowledge of Shareholder power of the Bongo Rural Bank**



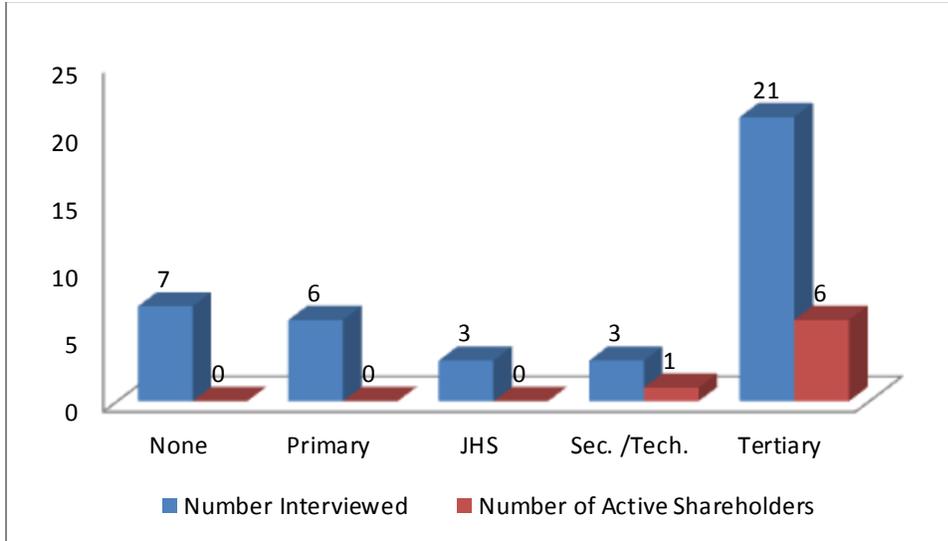
**Figure 2. Relationship between Level of Education and Knowledge of Shareholder power of the Naara Rural Bank**

### Shareholder Activism

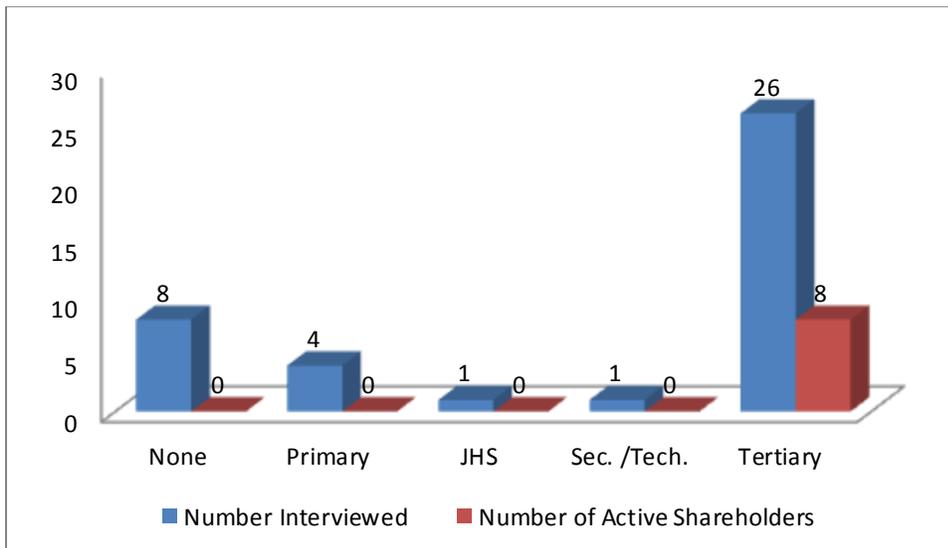
The researcher measured the general level of activism by analyzing responses to questions on the number of Annual General Meetings (AGMs) attended, whether they read all documents attached to the notice before attending an AGM, and their understanding and interest in issues discussed at general meetings; especially financial statements. The level of activism is a very important variable to drawing the conclusions for this research. For the purpose of measuring its prevalence among shareholders, the researcher first determined the category of shareholders that have a high degree of activism by measuring the relationship between level of education and level of shareholder activism, and between knowledge of shareholder power and level of activism.

**Level of Education and Shareholders Activism**

This relationship is a very important one to this research. The researcher has already established a relationship between high levels of education and level of awareness of shareholder power. The next important question therefore, is whether these people are exercising the power that they have and are aware of. A cross tabulation of these phenomena (as in figures 3 and 4) indicates that those at the second cycle and tertiary institutions are more active than those with lower levels and no education at all. As noted earlier, this is likely due to their exposure to a lot of other materials and that directly educate them about their rights as shareholders. On average, approximately 40% of those that are educated to the tertiary level are active and are much interested in how their investments are being managed.



**Figure 3. Relationship between Highest Level of Education and level of activism among Shareholders of the Bongo Rural Bank**



**Figure 4. Relationship between Highest Level of Education and level of activism among Shareholders of the Bongo Rural Bank**

**Knowledge of Shareholder Power versus Level of Activism**

The level of shareholders’ knowledge of their power has proven to be the panacea for shareholder activism. As seen earlier, shareholders who are educated up to the tertiary level tend to take more interest in seeking for knowledge, and therefore, have come across documents that explain to them the kind of power that they possess as shareholders. The relationship between level of knowledge of shareholder power and activism is presented in the table 2 below.

**Table 2. Relationship between Knowledge of Shareholder Power and Level of Activism**

| Level of knowledge | Bongo Rural Bank   |               | Naara Rural Bank   |               |
|--------------------|--------------------|---------------|--------------------|---------------|
|                    | Number interviewed | Number active | Number interviewed | Number active |
| None               | 21                 | 2             | 12                 | 0             |
| Little Knowledge   | 8                  | 2             | 19                 | 5             |
| Good knowledge     | 11                 | 3             | 9                  | 4             |
| <b>Total</b>       | <b>40</b>          | <b>7</b>      | <b>40</b>          | <b>9</b>      |

From the above tabulation, it is clear that those who are informed about the powers they possess as shareholders are active in participating in decision making where they have the chance to. An average of 30% of those who have little knowledge are active, while an average of 35% of those with good knowledge are very active in contributing to the effective governance of their banks. This means that although those who are aware of their powers as shareholders get involved in some form of activism, the majority is still dormant and will do nothing even if they know that things are not working the way they should. In order to further confirm this, the researcher used the Pearson Correlation Test to examine the relationship that exists between these two important phenomena. The emphasis is put on these two phenomena because the outcome of their correlation will ultimately form a major part in the conclusions drawn in this research. A correlation of 0.204 and 0.456 for the Bongo and Naara Rural Banks respectively goes to confirm the weak relationship between level of knowledge of shareholder power and level of activism among shareholders of rural banks. Most shareholders who demonstrated considerable amount of knowledge of shareholder power were still reluctant to invoke such powers due to general lack of interest.

**Shareholder Empowerment**

Findings from this research have pointed to the fact that when shareholders are empowered, there is the probability that they will use such powers to exert pressure on managers of their companies to be accountable. From the data gathered from the directors of the rural banks studied, shareholder can vote to determine who becomes a director of their banks. However, restrictions on board nominations mean that there are still some impediments on the way of shareholders when it comes to board appointments.

**Shareholder Education**

Shareholders of rural banks need some level of education (information) about the powers they possess and how they can effectively use such powers. Most of the respondents (on average 65%) who are aware of the powers indicate that they read about these powers themselves. About 20% were informed by the directors at general meetings, and the rest had heard about such issues from other shareholders.

The fact remains that, there is a weak relationship between knowledge of shareholder power and level of activism, but obviously, the more informed shareholders are of their powers; the more likely they are to get active as shareholders.

### **Shareholder Participation**

Although those who are highly educated are more informed of their powers as shareholders, they are not largely active in using these powers. Chizema (2011) noted that lack of shareholder involvement could be due to the fact that shareholders feel that they do not have sufficient power to influence corporate decisions. This notion is confirmed in this research, where some shareholders were having some grievances, but feel that the avenues for addressing such grievances are limited. A few of them noted that they had issues that they could have headed to court to seek redress, but they had neither the time nor the resources to do so. They generally feel that they do not have enough power to influence any actions of the directors; therefore, they prefer to remain silent and not take any interest in whatever the directors are doing.

### **RECOMMENDATIONS**

- Since most shareholders of rural banks are not highly educated, it would be appropriate to add shareholder education to the duties of customer service staff of the banks, so that they would be responsible for educating prospective shareholders on what they need to know before buying shares.
- There are some disparities in the framework of corporate governance among rural banks. The ARB Appex Bank, the overseer of rural banks in Ghana, needs to synchronise the governance systems of rural banks in order to achieve consistency in the manner in which these rural banks are governed, so that shareholders can be more empowered to influence the major decisions taken by directors.
- Rural banks should be encouraged to set up shareholder committees. If shareholder committees are set up, they could serve as lead advocates for these shareholders who are voiceless, and also serve as a platform through which their grievances can be sent to directors. The people who form these committees should be knowledgeable about shareholder powers and are ready to work for and on behalf of minority shareholders.

### **CONCLUSION**

Good corporate governance practices cannot be assured if external individuals and institutions do not closely monitor directors of companies who are supposed to adhere to these practices. Shareholders form a body that can effectively monitor the activities of directors since they have a direct interest in the institutions in which they invest. Most shareholders of rural banks are not aware that they possess some amount of power to influence decision making in their banks, and even to determine who becomes a director. A few of them know about these powers they possess, but are not showing any signs of interest in holding their directors accountable for their stewardship.

The researcher therefore, recommends that shareholders of Rural Banks need to be empowered more; shareholders should be given more education so that they get to know more about the influence they can bring to bear on the management of their resources, and finally, shareholder committees should be formed among those of Rural Banks so that they can serve as advocates for all shareholders.

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