DETERMINANTS OF PERFORMANCE OF PENSION SCHEMES IN KENYA: A COMPARISON OF UMBRELLA VERSUS INDIVIDUAL SCHEMES

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~~**BY**~~

WALTER WAFULA WEKESA

(MBA/002/16)

~~**RESEARCH PROPOSAL SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF DEGREE OF MASTERS IN BUSINESS ADMINSTATION.**~~

~~**SCHOOL/DEPARTMENT OF BUSINESS EDUCATION**~~

~~**KIBABII UNIVERSITY**~~

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June, 2020

ABSTRACT

Pension funds are the primary sources of retirement income to a lot of people in Kenya. The funds are also an important contributor to the country's gross domestic product (GDP) - pension assets as a percentage of GDP was at 13.4% in the year 2019. However, the current pension's penetration rate is still low at 20% and the growth of this industry is extremely pegged on attracting more people into the existing schemes. Exploring factors that determine performance of pension schemes in Kenya can guide the choice between schemes by potential pensioners in the country to make informed investment decision thus raising the penetration level. The goal of this study is to understand the determinants of performance of pension schemes in Kenya, comparing umbrella and individual schemes. Specific objectives that will guide the study include: i) to assess the influence of legal framework on performance of pension funds in Kenya; ii) to assess the influence of fund governance and ethics on performance of pension funds in Kenya iii) to assess the influence of investment strategy on performance of pension schemes in Kenya and iv) to assess the influence of operational efficiency on the performance of pension schemes in Kenya. Descriptive study design will be adopted. Study target population will include all the Kenya's 30 umbrella and 34 individual retirement schemes registered with the retirement benefits authority (RBA). A sample size of 256 participants will be engaged. These will comprise of 136 participants from individual schemes and 120 participants from umbrella schemes. 4 members from each scheme, with representations from the board of trustees, administration, fund manager and custodian will be purposively selected. These are the four levels that the RBA regulation requires for every scheme to have. The study will adopt a census approach and therefore data will be collected from all the 64 registered pension funds listed under umbrella and individual schemes. A questionnaire will be used to collect primary data from the selected respondents. The data collected will be analyzed using the statistical package for social sciences (SPSS) version 23.0 to produce frequencies, descriptive and inferential statistics which will be used to derive generalizations and conclusions regarding the schemes. Multivariate analysis will be used to measure the relationship between the independent variables and the dependent variable. The study findings will be presented using figures and tables comparing the two schemes. Findings will expectedly generate recommendations to the management of the two categories of the pension funds with an overall goal of attaining a sustained operational efficiency.

Proposed by:

Walter Wekesa (MBA/002/16.) **Sign …………….** **Date ……………..**

Supervisors

1. Dr. Munir Manini **Sign …………….** **Date ……………………………………**
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   Department of ………………., Kibabii University

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CONTENTS

LIST OF ACRONYMS AND ABBREVIATIONS

CALPERS	-	Pension fund covering local government workers in California
DB	-	Defined Benefits
DC	-	Defined Contribution
GDP	-	Gross Domestic Product
IMA	-	Investment Management Authority
KRA	-	Kenya Revenue Authority
M&A	-	Mergers and Acquisitions
NACOSTI	-	National Commission for Science, Technology and Innovation.
NHIF	-	National Health Insurance Fund
NSSF	-	National Social Security Fund
OECD	-	Organization for Economic Co-Operation And Development
PAYG	-	Pay-As-You-Go
RBA	-	Retirement Benefits Authority
RRTOF	-	Risk-Return Trade-Off Theory
TSP	-	Pension fund covering federal government workers in the United States.

LIST OF FIGURES

OPERATIONAL DEFINITION OF TERMS

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Pension Scheme: An arrangement or a plan which provides retirement income

Umbrella Schemes: Are schemes that bring together contributions of several employers and associated employees and thereby reducing the average cost per member and enhance overall returns and benefits to the members

Individual Schemes: These are schemes where individuals can contribute directly into the scheme towards saving for their retirement. The contributions are flexible in order to accommodate an individual's financial circumstances

CHAPTER 1: INTRODUCTION

1.1 Background of the Study

Pension funds have the objective of providing income in retirement. Individuals channel their savings earned during working days and invest them into the long-term financial assets for a better life in the post-retirement period. Members are protected from poverty risk in their old age because they from this investment, they have a livelihood beyond their working years. Members choose the plan in which they intend to invest their money and the fund managers for these plans trade with the contributions in money market. Upon maturity, the value of the money increases and the accumulated amounts are set in contributors' accounts from which the monthly pensions are later paid (RBA, 2016).

Kasanen, *et al.*, (2001), asserts that savings towards pension sustains the economy. Both the state, the institution, and the individual benefits from the higher return opportunities. Therefore, the state desires a growing number of participants in the pension scheme industry to boost resources to the economy (Murthi, 2015).

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In the Kenyan market, Retirement Benefits Schemes are categorized into two. The difference is in the mode of payment during retirement. These categories include pension schemes and provident funds. In pension schemes, both the employer and employee's contributions, together with the accrued interest can be utilized to acquire a pension annuity from an insurance company. This relies on the provision that the contributing member takes one third of the total amount as a lump sum. The balance goes towards the purchase of an annuity. On the other hand, a provident fund member acquires their total contribution plus accrued interest as a lump sum. The member has the say on how to utilize their funds (RBA, 2016).

Retirement benefit schemes can further be classified into two categories based on mode of contribution. Under this category, we can either have umbrella schemes or individual schemes. For umbrella pension schemes, the employees' and employers' contributions are pooled together. This leads to a reduction on the average relating to cost per member. Therefore, the members experience enhanced benefits and overall returns. Members in individual schemes on the other hand save for their retirement by making direct contributions to the scheme. In this type of scheme, there is flexibility for any individual financial circumstances. Kenya has 30 umbrella and 34 individual schemes registered with the RBA (www.rba.go.ke)

Strengthening of the third pillar of the pension industry which is, private and voluntary pension schemes, resulting from the individual funding has brought to the forefront questions as to the supervision and regulation of pension funds, the potential investment performance, and the administrative costs of pension funds. Schemes under private management are not under mandatory requirements to accommodate below-market returns with incentives that allocate capital to stocks and bonds with the best risk-yield combinations, whether these securities are public or private (World Bank, 2015). The projected benefits include international managerial expertise and international diversification of investments (Davis, 2012). However, when employers and workers lack adequate information to appoint a capable investment manager, problems may be witnessed. Additionally, privately managed funds are associated with higher marketing costs. Chances of benefiting from economies of scale are thus minimal as compared to publicly managed funds. Importantly, public funds require lower incentive than their private counterparts to achieve cost efficiency.

The motivation behind this study is based on various problems associated with the management of pension funds. First, comprising a variable number of institutions involved in the fund management, the industry has embarked on a wave of mergers and acquisitions (M&A) with an eye toward stimulating growth and gaining competitive advantages. This indicates that the market is facing strong competition, thus, necessitating efficiency to sustain performance (Barientos & Boussofiane, 2005). Secondly, the institutions operating in the pensions industry are highly heterogeneous occasioned by factors like ownership status, company size based on membership number, value, and type of pension fund managed. The heterogeneity is associated with the various management strategies with different market fortunes (Barros & Garcia, 2006). This may affect performance.

Finally, the taxation of retirement and long-term savings products change with time owing to a country's public deficits and the European Union's restrictions on public debt and budget deficits. The effects of this policy have direct impacts on pension funds management companies. Therefore, it affects the relative efficiency performance of the funds. Further, the different characteristics of such funds within the industry can also affect the above traits. This can lead to differences in performance from the varied strategies or different resources.

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The background must capture the global, regional and local context of the research problem. Its important to explain the literature of the phenomenon from developing countries perspective, Africa(regional perspective) and finally related studies in Kenya or East Africa

In this section, the researcher should define the context of the study by providing a brief discussion of key theoretical approaches and findings reported in earlier related studies. Trends related to the problem, unresolved issues and social concerns are discussed. Authoritative sources or citations should be provided in the section. It's important to the following:
- ☐ Should show understanding and genesis of the problem.
- ☐ Start with the global perspective followed by the local scenario.
- ☐ Should be approximately 5 pages (4-6 pages)

Should talk about the target population of the study

The closing paragraph to clearly show the knowledge gap your study will fill.
The is need to refine this section to give it the much needed vibrancy to capture the attention of the reader since it's the first section a reader encounters

1.2 Statement of the Problem

There has been a significant growth of pension funds in a number of countries globally. In Kenya however, the current pension's penetration rate is still low at 20 percent. The growth of this industry is highly pegged on attracting more people into the existing schemes. According to Agolla (2012), developing countries take longer to pay retirement dues, and in some cases, these dues do not get paid at all. Sometimes the dues are meagre. Odundo (2011) points out the need for good investment decision making that would bring back good returns under such circumstances.

There was a remarkable decline in returns on equity reported from 2011 to 2018, despite the increase in return on investment for the year ending June 30, 2013 (Coopers, 2016). Specifically for the years 2009, 2011 and 2012, there was a decrease in market values of the portfolios. Such inconsistencies in the industry's projected returns affect investment in stock and subsequently the general performance thus, calling for a systematic understanding of the contributing factors. Furthermore, the inadequate public information on financial markets changes affect the pension industry. This means, the clients lack tailor-made information to boost their investment decisions.

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Several factor have been associated with the performance of pension funds. As an example, Kinoti (2009) studied factors influencing pension fund managers' assets allocation decisions in Kenya. Using a panel data regression approach the study analyzed the global asset allocation behavior of pension fund managers regulated by the retirement benefits authority (RBA) in Kenya in the period 2001 to 2007. The study established the significance of legal framework in influencing fund managers' decisions even though its impact on other key performance parameters such as the efficiency of operation and investment strategy were minimally demonstrated.

Njuguna (2011) studied pension fund determinants in Kenya and how they relate to corporate governance in the country. While the study established that the governance of pension schemes is largely influenced by leadership and pension regulations, it was not conclusive as to whether governance in turn, directly influenced the funds overall performance. A study by Tonks (2005) on investment performance and pension fund management established an increase on the value of pension fund. This was attributed to the investment returns relating to the fund. Further, the investment strategy was solely responsible for the witnessed investment returns.

Identifying and understanding the persistence of the poor performance or good performance of an investment strategy is a vital issue and one in which further research would be worthwhile. Additionally, it is noteworthy that despite the related studies on pension funds' performance, none has attempted to compare performance determinants in umbrella schemes versus individual schemes in the country. To bridge this gap, this study aims at establishing various pension funds' performance determinants in Kenya while drawing comparisons between umbrella and individual schemes.

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The problem statement must indicate exactly what is the problem,how it a problem and why it's a problem. Its drafted on the basis of the background of the study

Note; Length – maximum 1 pages

1.3 Study Objectives

1.3.1 Main Objective

To assess the determinant factors of performance of umbrella versus individual pension schemes in Kenya.

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1.3.2 Specific objectives

1. To assess the influence of legal framework on performance of umbrella versus individual pension schemes in Kenya
2. To assess the influence of fund governance and ethics on performance of umbrella versus individual pension schemes in Kenya
3. To assess the influence of investment strategy on performance of umbrella versus individual pension schemes in Kenya
4. To assess the influence of operational efficiency on the performance of umbrella versus individual pension schemes in Kenya

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1.4 Research Questions

1. How does legal framework influence performance of umbrella versus individual pension schemes in Kenya?
2. How does fund governance and ethics influence performance of umbrella versus individual pension schemes in Kenya?
3. How does investment strategy influence performance of umbrella versus individual pension schemes in Kenya?
4. How does operational efficiency contribute to the performance of umbrella versus individual pension schemes in Kenya?

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1.5 Justification of the Study

The major responsibility of a pension contributor is to choose a fund manager and investment plan that suits the individual's situation and goals. There is a market competition among the fund managers, and they are interested in proving to offer the most beneficial services at the best prices. In this turn, a contributor has the choice to which manager to entrust their pension capital. In the financial markets, there are significantly varying investment opportunities, from safe investment in government treasury bills and bonds, to riskier, but potentially more profitable investments in companies` shares. Fund managers offers several plans with different levels of profit and risks that depends on what securities and deposits a contributor's pension capital will be invested. Therefore, before settling on an investment plan, one should have a clear understanding of performance of the diverse schemes available in the market and the determinant factors related thereof.

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The Justification of the Study should illustrate why the researcher is conducting the research and whom it shall benefit. In this section the researcher describes the values or the benefits that will accrue from doing the study. The significance of the study is concerned with the relevance of the problem both to the practice and theory. That is, does the study explore an important question, meet a recognized need or make a useful contribution to practice and theory. Much value is placed on doing research, which has primary value for the solution of practical oriented business problems.

1.6 Significance of the study

The findings of this paper intend to add to the body of evidence of contributing factors that determine performance of pension schemes in Kenya and specifically comparing two categories of schemes; umbrella and individual schemes. Further, it will heighten the awareness of potential pensioners and thereby act as a guide to decision making while settling for a fund manager. To future researchers, the findings will further provide a baseline information regarding the factors that determine investment performance of pension schemes in the country.

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1.7 Scope of the study

The study aims at assessing the overall performance determinant factors of all pension schemes in Kenya. However, an analysis of pension fund mobilization data for the various licensed pension funds administrators in the country since the contributory pension scheme was started in 1965 to date cannot be achieved due to time and resources constraints. Therefore, the researcher shall focus on umbrella and individual pension schemes which have been gained so much focus in the recent past in the pension industry. There are possibly several factors that influence performance of pension funds. However, this paper focuses only on the legal framework, fund governance and ethics, investment strategy and operational efficiency as explained earlier. 256 questionnaires will be adequately filled and returned by the target respondents to ascertain the variables of interest, these will be sampled from the existing 30 umbrella schemes and 34 individual schemes in the country registered with RBA.

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State exactly the geographical scope, time scope and the target population

The scope is the kind of a disclaimer. It should cite the focus of the study geographical area or target group/population/depth of focus in concepts or variables. In this section, the researcher describes the focus or scope of the study to enable an enthusiastic reader to make generalization of the findings.

CHAPTER 2: LITERATURE REVIEW

2.1 Introduction

The aim of this chapter is to appraise what other researchers have reported regarding the performance of pension funds and also associated determinant factors. Additionally, it seeks to appreciate shortcomings in similar research works that can be utilized while drawing comparisons with the present study.

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~~2.2 The growth of pension schemes~~

~~In the recent past, the pension fund has gained popularity globally, thus leading to an exponential growth and establishment in most countries. Consequently, the performance and management of the fund is on the spotlight. Statistical evidence demonstrates a rapid growth of pension funds in both industrialized and developing countries. By 2001, pension funds accounted for 45% of the G7's GDP (Chatterton *et al.*, 2010). Within the same period, pension funds contributed 20% of the third world's GDP. According to Antolín et al (2010), the enormous contribution in developing nation's GDP resulted from changes in demographic characteristics. Chatterton *et al.* (2010) state that pension fund complements capital market and steers a country's growth by providing capital for investment projects. In addition, the investment of pension funds benefits individuals and the economy, especially investment banks. Therefore, pension funds should be properly monitored to prevent them from short- and long-term benchmarks.~~

~~Meng and Pfau (2010) underscore the need for improved management of pension funds in many countries because the world's population is constantly increasing. This has made it challenging to sustain the traditional pay as you go pension system since the amounts contributed into the scheme by the working persons increasingly became insufficient to support the elderly. For this reason, countries have re-focused their pension systems. Additional to the key reasons of responding to the growing population and the inconsistent financial positions, other motivation behind countries re-orienting their pension systems included the very fact that pension funds contributes greatly to a country's savings and capital market development. The pay as you go (PAYG) system thus, became unsustainable and prone to political manipulation, and the benefits paid to retirees decreased.~~

~~Bettendorf and Heijdra (2006) while addressing pension crisis in industrialized nations noted that the percentage of the elderly population (65 years and above) within the working age (15-64years) was 12% in 1950, 21% in 2000 and predicted it to extend to 44% in 2050, thus threatening the sustainability of the PAYG system. According to World Bank (2015), the PAYG pension system contributed to intergenerational inequity since it merely transferred wealth from today's workers to today's retirees. In such means, the PAYG pension system transferred responsibility to the current workforce, forcing them to pay pension (taxes to support current retirees). At the same time, they must manage the responsibility of caring for the future generations (current childcare). The resulting cycle does not guarantee returns to the ageing population. In addition, the system could only be under the management of the government since private institutions had operational integrity issues as the population aged towards retirement.~~

~~2.3 Pension funds in Kenya~~

~~In Kenya, pension schemes have been in place since the period after independence in 1963. The first post independent pension fund body, the National Social Security Fund (NSSF), was established in 1965 (RBA, 2013). Before the imminent reforms, members benefited from the pension fund system upon attaining the mandatory retirement age of 55 (GoK, 2015). The guarantee was resolved to include the worker's full basic salary throughout their service life or that of the widow as the law did not envisage a situation where the wife would support the husband. This law was embodied in the NSSF Act and the pension Act (Cap 189).~~

~~There have been major changes in retirement benefits industry in Kenya within past years. These have led to an improved pension coverage of about 20% of the current working population, compared to 1997 when the industry was unregulated. The industry lacked protection of the interests of the members in management of scheme affairs. Lack of regulatory framework brought about some of the challenges facing the retirement benefits industry, prompting the enactment of the retirement benefits Act in 199. The missing regulations also encouraged arbitrary investment of funds without autonomous professional advice, embezzlement and mismanagement of scheme funds by trustees, schemes not being satisfactorily funded thus unable to fulfil their promises to people who are retiring in spite of members making their contributions and records being mismanaged (Retirement Benefits Act No. 3 of 1997; GoK, 2005; Income Tax Act Cap 487).~~

~~The benefits Act of 1997 thus created the RBA with the mandate of overseeing and regulating managements in the industry. Additionally, it streamlined developments and promotion of the retirement benefits sector. Remarkable growth has been witnessed in the industry since the enactment of the Act, especially in handling assets management, which stood at 1.2 trillion in June 2018 (KNBS, 2018). RBA has further promoted good governance by continuously updating and~~

~~enforcing the regulations. The regulation affirms that each scheme must have a minimum of service providers falling into four main categories including, corporate and board of trustees who owns the scheme and runs its affairs, an administrator handling daily accounting services of the scheme, a fund manager who executes the trustees' investment policy statement and a custodian holding the scheme's assets.~~

~~In Kenya, the industry includes the entire working population within the private and public sector. The system is comprised of three pillars. The zero pillar involves state funded pension for citizens above 65 years of age and provides them with a basic income. This falls under the management of the ministry handling social protection. The first pillar is a mandatory contribution from every worker and employee, whether in the formal or informal sectors. This is where the NSSF falls. And finally, the second pillar is majorly employer based and contributory for everyone except the civil service pension scheme and county schemes (RBA, 2016).~~

~~Individual and umbrella pension schemes in Kenya are mainly run by corporate institutions, commonly, insurance companies (RBA, 2013). These schemes are open to public and are convenient channels of retirement benefits including those in employment and those wishing for additional voluntary contributions. In cases were employers are not able to establish independent occupational schemes due to a smaller workforce, employers are encouraged to either put their employees on individual schemes or pull together with other employers in umbrella schemes. An individual's choice of investing in umbrella retirement benefits scheme or an individual retirement benefit scheme therefore largely depends on the nature of client's employment and employer's decision on whether to support such benefit like the case of umbrella schemes. This is because it~~

~~will upon the employer to make contributions on behalf of their employees while an individual determines and makes contributions on their own behalf.~~

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2.2 SHOULD BE THEORETICAL FRAMEWORK
The theoretical review is followed by the conceptual framework before the empirical literature. This literature review section of the proposal should present a review of the literature related to the problem and purpose. The literature review section should therefore be organized or categorized according to the research questions or specific objectives in order to ensure relevance to the research problem. It should be written using appropriate writing style of the American Psychological Association (APA) style. Cite 3-5 references per key section in the text. Review the empirical literature relevant to the problem being investigated showing clearly the linkage of literature review to the research questions.
During literature review, it's important to note the following points:
☐ You should *evaluate* what has already been done, show the *relationships* between different works, and show how it relates to *your* project.
☐ Refer to work by recognized experts in your chosen area
☐ Consider and discuss work that supports and work that opposes your ideas
☐ Make reasoned judgments regarding the value of others' work to your research
☐ Support your arguments with valid evidence in a logical manner
☐ Distinguish clearly between facts and opinions
☐ Ensure the review is done chronologically
☐ Each key variable should be 2-3 pages long.
☐ The hypothesized variables should be subheadings of the literature review to form a framework that would help in analysis.
☐ It is not supposed to be just a summary of other people's work but Critique of the existing literature relevant of the study
☐ Review and critique any previous studies. For the review to be critical, you will need to develop critical judgment.
☐ Indicate what has been done by other researchers including the methodologies used and identify the gaps.
☐ The emerging Research gaps.

2.4 Factors that influence performance of pension schemes

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2.4.1 Legal Framework

According to Davis (2012), regulation greatly influenced the management of pension industry. Such regulations have stabilized the financial systems by providing conducive environment for efficient resource allocation that subsequently promote economic growth. Pension funds were not prudently invested or managed before the introduction of the RA regulations hence the value of funds was not preserved. It became clear that government's intervention was necessary (Rono et al., 2010). The act devotes several sections to provide guidelines on pension funds investment and their management.

Kikete (2012) conducted a study on the effect of regulatory control changes regarding financial performance of pension schemes in Kenya. This study was aimed at establishing the effect of the regulatory control changes passed since 2008 to 2013 on the financial performance of pension schemes. The study adopted a cross sectional survey design on 1216 NSSF contributors. The collection of secondary data was achieved from the industry reports and analysis was performed using ratio analysis. Findings reported that if processing period of the benefits is reduced, and the charged by the service providers is regulated and allowing access of 50% of the employer's portion have an influence in financial performance of pension schemes in Kenya. The design of the study, however, did not allow for a comparison of the impact of these factors across the different types of schemes available in the country.

According to Ngetich (2012), the government can intervene with a policy to obligate employers to provide certain benefits to employees. The government can for instance use the national assembly to legislate laws that enforce payment of the benefits. The law will make it mandatory for employers to pay certain benefits to the employee. Some types of employee benefits in Kenya are mandatory as they are a requirement by the law while others are optional. The legally required benefits include for example various kinds of insurance covers for the workers. The NSSF Act Cap 258 in Kenya for example, obligates employers to enroll employees into the social savings plan whereby the employer matches the employee deduction to be paid upon retirement. Moreover, the National Health Insurance Fund (NHIF) Act cap 255 obligates both the private and public sector employees to obtain NHIF medical insurance cover. The employer is given the mandate to deduct the premiums for the employee and remit it to NHIF.

Murthi (2015) noted that regulation improves governance of pension schemes. He argues that for private arrangements, whether individual or enterprise, regulation is essential in protecting beneficiaries and increasing transparency. His study is however silent on whether regulations directly impacts the overall fund performance. The lack of details about returns, balances and costs in most private pension schemes always restricted comparisons among beneficiaries. While private pension arrangements are often provided by insurance companies, their regulators hardly demonstrate the expertise to monitor the fund providers. In Africa, interference by government has also been a key issue in pension funds management. This is motivated by the design of the institutions which enables control by government, boards and administration and has been the motivation behind reforms in the industry.

2.4.2 Investment strategy

According to Stanko (2002), and an investment strategy is the assortment of investments made by pension funds, the study firms that investment strategy determines the investment mixture of the total funds of the pension that aims to have a careful balance between investment risks and returns. Investment strategy is therefore a plan that guides the choice of investments that pension funds make. Rono (2010) argues that there is a positive relationship between risk and returns. A pension fund will take more risk for better returns. It is therefore suggested that pension funds adopt appropriate investment strategies that provide higher returns on investments with moderate risks.

The type of pension fund determines the investment strategy. This is according to OECD (2016). However, the overall goal of any strategy is to maximize returns generated. This means, that the investment strategy and subsequently the returns, may possibly have an impact on financial efficiency as well as the overall fund performance. An effective investment strategy is based on four pillars namely, the prudent person rule (ensuring that all investments made are in the best interest of members), diversification (ensuring that the pension investments are not concentrated in a very specific asset), maturity matching (ensuring that investments mature as the liabilities become due) and it should have a transparent statement policies (Kyiv,2003). Since 200, there have been poor global market performance that has led to a shift in investment strategies. Institutional now incorporate additional fixed interest securities at the expense of equity investments (OECD, 2014b). It is supported that the motive has been to mitigate the low returns experienced on equity.

Therefore, strategic decision making relates to the investment strategy through the setting of parameters based on institutional performance. Further, it helps the institutions match their goals and objectives and focus on achieving long-term investment strategies. Owinyo (2017) observes that strategic decision-making attracts higher returns that improves efficiency. When applied consistently, a good investment strategy yields more returns with minimal risks for the individual pension funds. To achieve pension fund efficiency, pension funds must devise sound investment strategies and apply them consistently.

Investment strategy guides the institutions towards the attainment of pension fund's short term (<3 years), intermediate (3-10 years) and long term (>10 years) goals. (OECD, 2014b). It also determines both the short term and long-term sustainability of a pension fund. That is, the strategy avails necessary environment for implementing financial instruments. This is achieved by incorporating the expected maturity of liabilities. An appropriate strategy would therefore ensure that a pension fund maintains firm grounds in various situations like during stock market volatility. The strategy ensures that the timing of transactions is met by the management, that is, "the strategy relating to buying and holding of investments such that assets are purchased when prices are low and short-term ones are disposed of when prices are high" (Kakes & Broeders, 2006).

Njuguna (2011) observes that better re-investment plans are only realized through proper company investment strategy. These plans benefit from the compounding effect through ploughing back the earnings. In addition, an investment strategy also earns from the taxation of investment returns. Furthermore, should the investment opportunities be restricted, the financial performance will be depressed, thus making the pension funds less profitable. An inadequate investment strategy is thought to lead to less wealth. Elton et al (2010) reported that "poor investment strategies led to a

53% less benefits to pensioners within the US as compared to a market portfolio over a 20-year period. On the other hand, proper investment strategy resulted in better performance of the CALPERS (pension fund covering local government workers in California) and TSP (pension fund covering federal government workers in the US)."

Supporting the above literature, Oluoch (2013) agrees that pension fund efficiency can be maximized when sound investment decisions are in place. Nonetheless, it is important to note that the aspect of risk remains a critical issue in investment strategy and that the risk element limits pension funds from investing their entire pension finances in very high return assets forcing them to invest in inefficient portfolios that blend high return with low return security (Murthi, 2015).

2.4.3 Fund Governance and Ethics

Over the past decades, studies have established positive links between better corporate governance and firm market value and performance (Andrews, 2006). Empirical research has contributed little attention to the impact of the governance structures in individual and umbrella pension schemes on performance of these funds. In contrast, the theoretical model of Besley and Prat (2013) proved that governance structure matters in defined benefit and defined contribution pension plans with respect to three potential sources of agency problems; the responsibility for monitoring the asset manager, asset allocation and the plan's level of funding.

Besley and Prat (2013) model proposes the various means to govern pension funds. For instance, in a DB plan, a set retirement benefits are offered to the beneficiary after considering their number of salaried years, cost of living adjustments, among others. Such benefits remain constant with performance involving assets of the members. The funds are usually owned by the institutions. As a result, any poor investment performance amounts to risks in the respective firms. Therefore, the imminent misunderstanding that might be witnessed between the fund owners and the beneficiaries are minimized. However, in the case of a DC plan, the situation is different. The retirement benefits received by the beneficiaries is calculated from their accrued contributions and the investment performance of the funds. Similarly, the profitability of the fund is independent on the capacity of the assets' investment performance under the beneficiaries' profile. The governance structure thus plays a role since the funds lacks the contracting ability. From the Besley and Prat model, the beneficiaries can only monitor and control the contributions of the trustees if optimal governance structure is in place.

Gillan et al. (2016) highlighted that both the internal and external aspects of governance as substitutes. Where the external governance is unreliable or weak in managing the pension funds, then the importance of internal governance can be utilized. Ambachtsheer et al (2012) further added that board characteristics, that lies under the internal governance, contributes to good firm performance. Since agency conflicts differ between companies, separating control and ownership in pension funds is usually an effective practice (Besley & Prat, 2013). What matters is that there should be clear definition of bears the risk in the pension funds. For example, the risks belong to the beneficiary in the case of DC pension plans. Therefore, their impact to monitoring body should be strong and reliable. That is, in every management decision, the contributions of the outside directors must be considered in representing the beneficiaries. Since the directors are duly elected by fund owners, their independence in dispensation of duties is thus hindered. Therefore, the importance of other governance factors can also be realized.

Hugman(2008) explains ethics as benchmarks of conduct that indicate how individuals should behave on moral duties and virtues, which themselves are originate from principles of right and wrong. According to the social investors' forum (2017), an ethics framework considers trustees as individually and collectively bound by the statuses, common law, and fiduciary responsibilities to the registered members of the pension fund. As a result, in every decision-making aspect, trustees must adhere to the ethical requirements that binds them. Ethical investing requires that institutions assess the extra financial risks that might arise from the investments, including the social, environmental, and corporate governance variables (OECD, 2013). Firms, including pension funds have witnessed continuous screening for unethical investing. Rono (2010) differentiated between positive and negative screening regarding the pension fund investments. He defines negative screening as the practice of avoiding or divesting the shares of companies with poor social, environmental, and ethical performance.

Empirical studies on fund ethics have reported mixed results on its influence on fund performance. Clark et al (2010) explored the link between pension fund trustees upholding ethical behavior and also the achievement of long-term objectives of the deed of trust. However, according to Ambachtsheer *et al* (2012), there is no existence of unethical behavior in pension funds in decisions relating to investments, benefit promises, and performance.

2.4.4 Operational Efficiency

Contemporary thinking in performance management is that organizations must not only increase resources but make better use of it (Canadian Institute for Health Information, 2014). This needs organizations, including pension funds, to be efficient and focus on those management activities that are within their control while using minimal resources (Sarkis, 2002).

Efficiency is defined in production economics the organization's ability to maximize resources to deliver products and services at a cost-effective basis without compromising on its objectives (Hackman, 2008). Pension funds are required to be efficient since they operate in a trust or fiduciary relationship with beneficiaries and expected to deliver adequate and optimized retirement benefits (Barrientos & Boussofiane, 2005). Globally pension funds have attracted the attention as a result of the volatile markets and also the consequent erosion of member's retirement values.

Globally pension funds have attracted attention due to volatile markets and the consequent erosion of member's retirement values. Therefore, understanding the relationship and efficiency of these factors is important for pension funds trustees to make informed decisions aimed at optimizing member retirement values.

Pension scheme operational efficiency is essential as it yields higher investment returns and consequently high retirement benefits to the pensioners (Bateman and Mitchell, 2004). However, inefficiency results to high costs of operation, lesser investment returns and also reduced funds (Bikker an Dreu, 2009). Closure of pension funds and low investment returns reduce the latter's contribution to the GDPs of countries (Njuguna, 2010).

Muhittin and Reha, (2014) argue that to drive operational efficiency in the industry, factors like supply chain management, operational aspects of human resource management, quality control management and technology deployed must be implemented adequately. Scheraga (2016) adds that the contributions of both public perception and customer satisfaction must be accounted acknowledged.

It can be noted that previous research findings on efficiency of financial institutions still leaves gaps that need to be bridged. For instance, numerous studies focused on mainstream developments of efficiency concepts in developed markets. A focus of efficiency research has shifted to fast growing countries while efficiency spill-over effects. This could not have been realized if smaller emerging markets would have not been broadly explored. However, research on smaller markets still leaves room for future exploitation since it comprises scientific value in future. The current study will expectedly contribute to filling this gap.

2.5 Theoretical Framework

Like other organizations, pension funds are considered open systems. This is because they collect and accumulate membership and sponsors' contributions, that is, employers who established the pension fund. The contributions are then invested, and proceeds held in stewardship to benefit the members upon retirement. A close examination thus agrees that pension schemes work as systems (Chansam, 2015). This is because the funds receive contributions that they convert to benefits; equivalent to any system that receives inputs and converts to outputs.

According to Owinyo (2017), pension funds' financial performance is a useful element in determining net income and is also instrumental in assessing organizational financial risk. Retirement benefit schemes' financial performance can be assessed by evaluating the increase in income streams. The main source of funding for retirement benefit schemes is contributions received. Blome et al (2010) stated that other source of income for pensions include the net returns made from investment of the contributions.

This study is based on three theoretical foundations; the theory of risk-return trade-off, the theory of constraints and the stakeholder theory. These theories are applicable in understanding performance of pension schemes fund. The factors determining performance of pension funds may be hindered or accelerated by constraints either from management or stakeholders in goals setting of the schemes which have a pervasive influence on performance in organizations and management practices. The pension industry sets goals by the respective managements but may be delayed by constraints during performance of the organization.

Commented [MM24]: ARE THESE THEORIES RELEVANT TO THE STUDY

2.5.1 The risk-return trade off theory

The risk-return trade off theory (RRTOF) was advanced by Leon, Nave and Rubio in 2005 and it highlights the relationship between investment decisions and risk-return trade off. According to RRTOF, risk-return trade-off forms the foundation of financial economics and is a long-standing event in investment analysis. To assess an investment potential returns, one must establish the perceived risk of venturing into any given investment. This also affirms the direct relationship between return and market risk since additional compensation is required for risk-averse investors assuming extra risk. Therefore, investors associate high risk markets with high returns. This is for purposes of compensating the risk involved in investing in such markets. Contrary, lower risk markets are characterized by lower returns. The risk-return relationship is thus an essential concept in investment decision making and can be accepted as the cornerstone of rational expectations of asset pricing models (Leon et al, 2005).

According to Hubbard (2009), a risk is the expectation that the actual returns of an asset will be lower than the expected returns. A tradeoff must thus be identified to establish the link between risk and expected return. Investment in risky asset are accompanied by higher return, than for example, a risk-free investment. Expression of this relationship takes a variety of ways. Fama and French (2004) developed capital pricing models to explain the relationship between expected return and risk associated with an investment. The model illustrates how assets can be valued taking into account the risk associated with the asset.

Elton et al, (2010) explains the three concepts that apply in the capital asset pricing model (CAPM). First, higher risks yield higher returns. Secondly, return is positively linearly connected to risk, that is, as risk increases, return also equally increases. And lastly, unsystematic risk is not rewarded. This is because it can be easily diversified away. However, the theory does not put into consideration unexpected changes and outliers in the market. This means that anticipated returns could be immensely affected, and vice versa. Therefore, according to the study, the risk-return trade-off theory is important in guiding decisions around investment strategy, fund governance and operational efficiency of a pension fund. Since fund managers understandings better the risk dynamics, they can make investments that yields more returns at lower risk. However, this does not mean that pension managers do not take risk. They should do so, but as this happens, the funds at their disposal should be safeguarded through investment in diversified asset and products.

2.5.2 The theory of constraints

The theory of constraints, as developed by Eliyahu Goldratt, addresses systems-management philosophy since its recognition in the early 1980s. Its fundamental thesis supports that the performance limits for any system is established by constraints. Most organizations or firms contain a few core constraints. The theory advocates that managers should focus on effectively managing the capability and capacity of such constraints to improve the organizational performance. Once considered simply a production-scheduling technique, theory of constraints encompasses wider application margins in diverse organizational settings (IMA, 1999).

Theory of constraints stresses that managers must rethink their fundamental assumptions on how to realize their organizational goals by focusing on productive actions and cost management purposes. Emphasis is laid on measures that maximize throughput revenues earned through sales. Further, the theory focuses on developing an understanding on how to manage the constraints that stand between an organization and the attainment of its goals. After identifying the constraints, theory of constraints, all the non-constraining resources of the organization are subordinated to meet the needs of its core constraints. This ensures the total system of resources are optimized (IMA, 1999). At the backdrop of this theory, the current study investigates performance determinant factors of umbrella versus individual pension schemes in Kenya.

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2.5.3 The stakeholder theory

According to this theory, corporate institutions are obligated to ensuring that all stakeholders at different levels are satisfied based on their respective expectations. The theory defines stakeholders as groups and individuals who feel the impact of the intervention – both the benefits and demerits. These may include but not limited to shareholders, creditors, employees, customers, suppliers, and the community at large. The theory therefore asserts that management as the role to not only involve stakeholders at the decision making level but also those impacted by business decisions. This theory is thus applicable to understanding determinant factors of performance of pension schemes with an overall goal of increasing access of pensions to members.

2.6 Conceptual Framework

The figure 2.1 shows a roadmap of the major concepts associated with performance of pension scheme funds and their inter-relationships. The synergy shows a relationship between the independent and dependent variables.

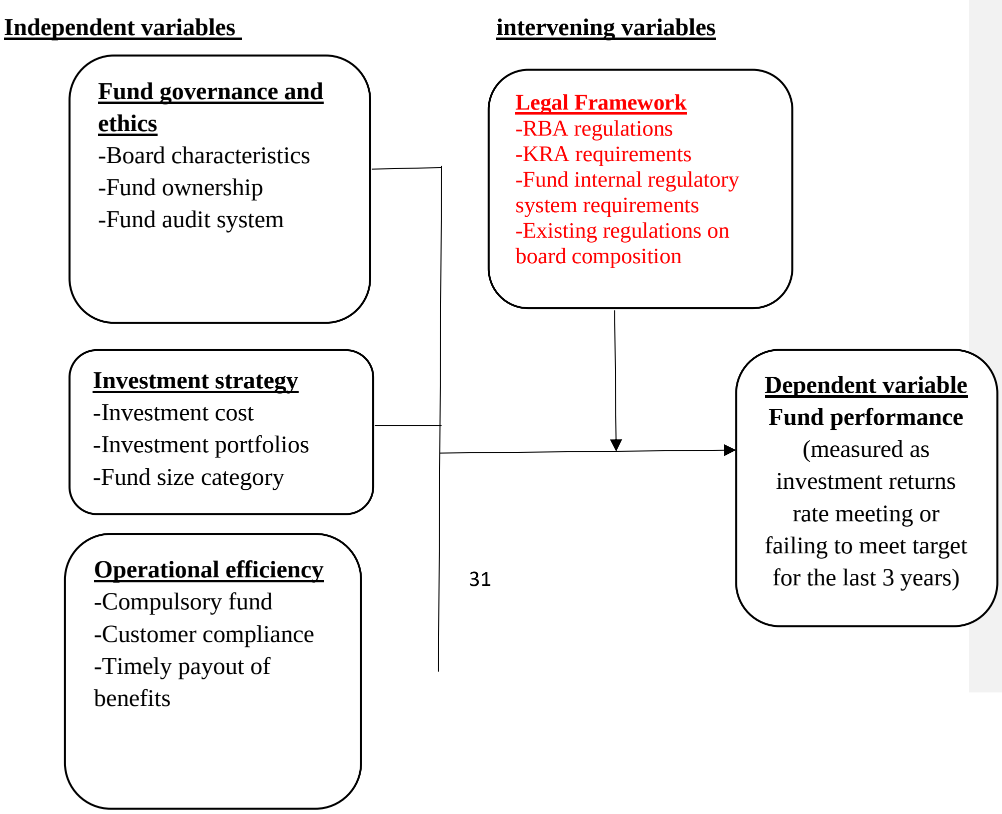

Figure 2.1. Conceptual framework diagram

2.3 CRITIQUE OF THE EXISTING LITERATURE RELEVANT TO THE STUDY

2.4 SUMMARY

2.5 RESEARCH GAP

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This sub-section is supposed to summarize the literature reviewed and bring out clearly the research gaps identified, if possible in a table format

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CHAPTER 3: METHODOLOGY

3.1 Introduction

In this chapter, the procedures which will be adopted This chapter describes the methods, techniques and procedures that will be used to answer the research problem. It gives a description of the research design, population, sampling techniques and data collection and analysis procedures that will be used.

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3.2 Research design

This study will adopt a descriptive research design. Descriptive research involves gathering data that explains more about the events and then organizes, tabulates, depicts and also describes the data collection. The design is considered fit because the study in question seeks to collect and analyze data from a population at a specific point in time. It will involve collecting data from members of a population in order to determine the current status of an event (performance of pension schemes) with respect to more than one variable. The study will be a survey since the researcher has no control on the factors influencing performance of pension schemes. The major emphasis will be to determine the frequency of occurrence or the extent to which variables are elated.

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3.3 Target Population

The target population for this study will be 256 participants. This will comprise of 136 participants from individual schemes and 120 participants from umbrella schemes. There are 30 umbrella and 34 individual retirement schemes registered with RBA in Kenya. The study will feature all the 64 schemes, engaging 4 members from each scheme – with representations from the board of trustees, administration, fund manager and custodian. These are the four levels that the RBA regulation requires for every scheme to have.

3.3 Study Variables

In the proposed study, dependent variable will be fund performance, measured as investment returns rate either meeting or failing to meet target for the last 3 years. On the other hand, independent variables investigated in this study will include; fund governance and ethics, investment strategy and operational efficiency. Under fund governance and ethics, the study will look at aspects of fund ownership, fund audit system and board characteristics. Investment strategy factors will include investment cost, investment portfolios and fund size category. Lastly, operational efficiency will feature aspects of compulsory fund, customer compliance, and timely payout of benefits, administrative costs and compensation package. Legal framework will be categorized as an intervening variable for the dependent and independent variables. Under this, the study will consider RBA regulations, KRA requirements, fund internal regulatory system and existing regulations on board composition.

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3.4 Sampling technique

This section describes the sample size and the sampling procedures used to obtain a sample for the study.

3.4.1 Sample size determination

The study will entail a census of all the 64 schemes. Representations will be obtained purposively from the board of trustees, administration, fund manager and custodian of each fund making the number of participants 4 from each scheme, thus a total of 256 participants for the study.

3.4.2 Sampling procedure

First, census sampling method will be used to select all the 64 umbrella and individual schemes. Purposive sampling will then be adopted to select a member from each of the four sectors outlined as mandatory for a scheme in the RBA Act.

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3.5 Data collection instruments

The study will rely on primary data which will be collected using a questionnaire.

3.5.1 Questionnaire

In this study, a questionnaire will be used to collect data from the respondents. Both open and close-ended questions will be used. The questionnaire will be self-administered and will be issued either via email or on a drop and pick later method to the respondents. Follow up will be done by calls to ensure all the respondents hand in their responses.

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The questionnaire will be developed an organized on the basis of the research questions or the specific objectives to ensure relevance to the research problem. This will also improve validity. The instrument will then be subjected to review by an expert, followed by a pilot test for reliability and statistical conclusion validation.

The structure of the questionnaire will be as follows: Part one will capture demographic information of the respondents in terms of job related profile, experience and organization profile. Part two will focus on the first objective featuring pension fund governance and ethics. Questions in this section will focus on fund ownership, fund audit system and board characteristics. Part three will focus on investment strategy and questions in this section will revolve around investment cost, investment portfolios and fund size category. Part four of the questionnaire will contain questions on operational efficiency, featuring compulsory fund, customer compliance, and timely payout of benefits, administrative costs and compensation package. The last section will address legal framework issues such as RBA regulations, KRA requirements, fund internal regulatory system requirements and any existing regulations on board composition.

3.6 Pre-testing of data collection tools

3.6.1 Pilot Study

In order to check applicability of the questionnaire, it will be piloted on a group of 25 pension scheme administrators. This is 10% of the study sample size (Connelly, 2008). This will be conducted prior to the main data collection exercise. In the process, the researcher will check for vagueness and familiarize with content of the tool. Any adjustments will be made before the actual data collection. A revised questionnaire will thus be adopted and dispatched to the target population. The pilot population will not comprise the study sample.

3.6.2 Validity of Data Collection Instruments

According to Mugenda & Mugenda (2003), validity is the accuracy and meaningfulness of inferences, which are based on the research results. This refers to whether the research instrument truly measures that which it was intended to measure or how truthful the research results are. The validity of research instruments in this study will be tested through expert opinion from the supervisor to determine the possibility of flaws, weaknesses and ambiguities in any of the question. Adequate corrections and revisions will be undertaken to enhance validity of the instrument.

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3.6.3 Reliability of Data Collection Instruments

Reliability is that the degree to which a tool produces stable and consistent results. To test for reliability of the data collection instrument in this study, internal consistency will be calculated from pilot study data by split half method to obtain the correlation coefficient (r). A coefficient of 0.7 and above is going to be considered.

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3.7 Procedure for data collection

First, permission to carry out the study will be sought from the National Commission for Science, Technology and Innovation (NACOSTI) as well as from the University. Eligible participants will then be identified and contacted with the help of trained research assistants through email. Each study participant will be requested to respond to the questionnaire that will be sent together with a letter of consent request. Filled questionnaires will be submitted back for checks and follow up will be done for non-responses.

~~3.8 Procedure for data analysis~~

~~SPSS and Microsoft Excel will be used as the data analysis tools for this study. Once filled forms are submitted, the entries will automatically be saved into a google spreadsheet and imported into SPSS for analysis.~~ Inferential and descriptive statistics will be utilized. Descriptive statistics will be used to summarize data and describe the sample, while the inferential statistics will enable the researcher to infer the sample results to the population. At this stage, chi-squared test at $\alpha = 0.05$ (95% confidence interval) will be used to investigate the association. Data will be presented in tables and graphs. All independent variables that will show statistical significance from the chi square analysis will be introduced into a logistic regression model to examine the degree of the relationship between the variables.

3.9 Ethical consideration

Approval to carry out this study will be obtained from NACOSTI. Approval from the university will be sought too. Administrative clearance will also be sought from the firms involved. Informed consent will be obtained from participants before the administration of the research questionnaire. The consent will be a written form with details on ethical considerations, procedure of the study,

Commented [MM35]: SHPULD BE CAPTURED UNDER DATA COLLECTION SECTION. This section describes step by step which will be followed in data collection. It should discuses which method(s) to be used to address Validity and reliability of the study instruments. Such methods include pilot-testing, Cronbach alpha, test-retest method among others. Beside this the researcher should discuss the method of administering the data collection instruments, justify the use of such method. Issues related to research permit, research assistants should also be discussed. Finally the research should state the approximate time required to collect the data.

Commented [MM36]: This section should present detailed steps of how the quantitative and qualitative data will be analyzed. For quantitative data it should included descriptive statistics and inferential statistics to be used, also show which of these will be used for which objective or hypothesis. Descriptive statistics include frequencies, measures of central tendencies (mean, medium or mode) and measures of dispersion (standard deviation, range or variance). Inferential statistics involve measurement or relationships and differences between or among the variables. Inferential statistics include correlation, regression and analysis of variance among others.
The qualitative data analysis technique used should be content analysis. The candidate should also explain how Type I and Type II errors will be controlled. In addition, the researcher should include, the procedures used to examine the variables and steps taken to control for extraneous influences that might threaten the findings of the study. Finally the section should explain how the results of data analysis will be presented and justify why use that specific method of presentation.

confidentiality, benefits, risks and the right not to participate or withdraw at any time. Respondents will be requested to sign and keep a copy of the consent form.

All anticipated risks and discomforts will be explained to the participants in the consent. The participants won't be paid for their participation in the study. All the information they share will be kept confidential. Participants' information will be protected, and all identifiable information will be encrypted and stored on password-protected computers. No individual identities are going to be used in the reports or publications which will result from this study. The decision to participate in this study will be personal. Participants will be free to take part in the study or not. If they decide to join, they will also be free to change their mind and stop their participation in the study at any time for any reason. There will be no penalty for such, and this will be clarified in the consent form.

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REFERENCES