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The Relationship between Board Characteristics and Dividend Payment Policies in JSE Top 40 Listed Companies

by

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Declaration of originality work

“I, **Tatenda Nharo** declare that this minor dissertation is my unaided work. Any assistance that I have received has been duly acknowledged in the minor dissertation. It is submitted in partial fulfilment of the requirements for the degree of MASTER OF COMMERCE in FINANCE at the University of Johannesburg. It has not been submitted before for any degree or examination at this or any other university.”

TATENDA GETRUDE NHARO

Signed

19 OCTOBER 2020

Date



Abstract

There are mixed findings on the factors that impact dividend payout in emerging market economies. It is well established in literature that corporate governance affects the level of dividends paid out by a firm. Even so, it remains unclear whether dividend payout is an outcome or a substitute of effective governance.

Against the background of the agency and resource dependence theories as well as the outcome and substitute hypothesis, this study applied panel regression analysis to investigate the relationship between corporate governance board characteristics and dividend payout (dividend payout ratio), for a sample of 29 firms in the top 40 of the Johannesburg Stock Exchange (JSE). The study was conducted for the period 2013 – 2018. The main contribution of this research to the extant literature was envisaged to be the introduction of a wider variety of variables. These additional variables, namely board gender diversity, board ethnic diversity, financial expertise and the average age of the board members, became the main focus of this work. Four control variables were used in this study, namely board size, board independence, profitability and previous dividend.

Significant relationships between board ethnic diversity, board independence and the dividend payout ratio were observed. Strong evidence presented in favour of the substitution hypothesis where JSE top 40 boards with a higher degree of independence did not need to use dividends as a tool for monitoring managerial behaviour. Furthermore, evidence supporting the maturity and dividend smoothing theories was observed through the significant relationships between profitability, previous dividend and the dividend payout ratio. The results are consistent with those in previous literature and have contributed to the extant literature seeking to establish the determinants of dividend payout policy in South Africa.

Key words

Dividend, dividend payout ratio, JSE top 40, corporate governance, board of directors, outcome, substitute, agency theory, resource dependence theory, panel regression

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List of abbreviations

AVAGE - Average age of board members
BBBEE - Broad-based Black Economic Empowerment
BETHN - Board ethnicity
BFINEX - Board Financial Expertise
BGEN - Board gender
BIND - Board Independence
BSIZE - Board Size
CEO - Chief Executive Officer
CFO - Chief Financial Officer
CG - Corporate Governance
DOA - Department of Accountancy
DPR - Dividend Payout Ratio
EPS - Earnings per Share
GDP - Gross Domestic Product
HSRC - Scientific and Industrial Research Council
JSE – Johannesburg Stock Exchange
NED - Non-Executive Director
OLS - Ordinary Least Squares Method
PREVDIV - Previous dividend
PROF - Profitability
ROA - Return on Assets
SABS - South African Bureau of Standards
SME - Small to Medium Enterprises
SOX - Sarbanes Oxley Act
UK - United Kingdom
US - United States

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Chapter 1 Introduction and Background

1.1 INTRODUCTION

In the last few decades, dividend policy has remained a controversial subject in corporate finance. Many finance academics have sought to examine and understand why firms make the decision to either pay or withhold dividends. It seems obvious that shareholders who risk their finances by investing into a firm should be rewarded by means of a dividend payout. However, it appears prudent for an entity to withhold dividends for the purposes of investing in other lucrative opportunities that would increase the wealth of its shareholders (Black, 1976).

In reality, the dividend decision has turned out to be more complex. Black (1976) concurs that the question of dividends is often more complicated than thought. In this regard, Black (1976, p.5) posits that 'the harder we look at the dividend picture, the more it seems like a puzzle, with pieces that don't fit together.'

Lintner's (1956) initiation of the dividend debate has led to many conflicting theories that have made it harder to derive sense of the factors that explain or determine dividend policy. Consider the maturity perspective brought forward by De Angelo, De Angelo and Stutz (2006) in which they hypothesised that mature firms are most likely to pay out dividends as they are more profitable and are less inclined to seek out multiple investment opportunities with their earned capital overtime. This has not been the case with 15-year old company Facebook, an entity that has subjectively matured and enjoyed lucrative earnings over the years (Caplinger, 2019). By July 2020, Facebook was yet to pay its first dividend despite growing expectations of a dividend payout within financial markets (Nasdaq Stock Exchange, 2020). The Facebook story provides a contrasting reality to the maturity theory proposed by De Angelo et al. (2006), thus reflecting on the complexity surrounding dividend decision matters.

Al Najjar and Kilincarslan (2018) underscore three main views that have been adopted by previous research on the importance of dividend policy, namely that 1) dividends are irrelevant to firm value, 2) dividends are relevant to firm value and 3) dividends are counterproductive to firm value.

In the first view, Miller and Modigliani (1961) propose that dividends are immaterial when considered under the presumption of perfect capital markets. They were confident that dividend payments added no contribution to the overall value of a firm. Against this background, Miller and Modigliani (1961) emphasise that firm value was created by the earnings generated from investments rather than the distribution of these earnings.

In the second approach, Gordon (1959) refutes Miller and Modigliani's (1961) stance by suggesting that shares were less risky in a firm that paid dividends due to an increased certainty regarding cash flows. The reduction of risk would subsequently raise the share price of the dividend paying firm, thus increasing firm value (Gordon, 1959).

According to Al-Najjar and Kilincarslan (2018), the third view is that the payment of dividends can be counterproductive to the creation of firm value and maximisation of shareholders' wealth. Brennan (1970) argues that the uneven balance in the treatment of capital gains tax and dividends tax influences an investor's choice to receive dividends or forfeit payments in favour of capital gains. In the event that there are greater tax advantages tied to capital gains, investors may prefer to accept fewer or no dividends; therefore, it may be better for firms to pay less or avoid dividends in order to increase firm value (Brennan, 1970). The payment of dividends might increase the tax burden on the investor, causing the investor to seek investment in a non-dividend paying firm (Brennan, 1970; Elton and Gruber, 1970).

From these three main approaches, several theories have emerged in attempts to explain why firms pay dividends. One of the most widely used explanations is the agency cost theory. Jensen and Meckling (1976) propose some of the earliest literature on the 'agency cost theory' which emanates from the divorce of ownership from control and the disparities between managerial and shareholders' priorities. According to Jensen and Meckling (1976), managers prefer to issue out lower dividends so that they can pursue investments of their own preference, rather than to maximise the share price. Jensen and Meckling (1976) argue that high dividend payouts reduce the amount of cash free flow that is available at the discretion of managers; hence, it forces them to interact with the capital market to fund new investment projects and it induces monitoring by the market.

Apart from dividends, an additional system that safeguards against the agency problem is corporate governance. "Corporate governance is, to a large extent, a set of mechanisms through which outside investors protect themselves against expropriation by the insiders" (La Porta, Lopez-de-Silanes, Shleifer & Vishny, 2000, p.4). The system incorporates the board of directors as an important mechanism to exercise control over senior management

and ensures that decisions made support the maximisation of shareholder value rather than the interests of senior management (John & Senbert, 1998). In addition, the board has many other fiduciary duties, including but not limited to dividend policy decisions (Abor & Fiador, 2013).

Broadly speaking, dividend policy literature focuses on three main aspects, namely 1) theory development such as the 'irrelevance theory' by Miller and Modigliani (1961) and the 'bird in the hand' theory by Gordon (1959), 2) the determinants of dividend policy and 3) research seeking to increase the prediction accuracy and modelling of dividend payments (Elyasiani, Jia & Movaghari, 2019). This study contributes to the second group, focusing on corporate governance as one of the determinants of dividend payout. The research focus is narrowed to the relationship that exists between significant board characteristics and dividend payout in the Top 40 companies listed on the Johannesburg Stock Exchange (JSE).

1.2 BACKGROUND TO THE STUDY

The renewed interest in corporate governance studies focusing on board characteristics has been fomented by increased corporate scandals and failures that have transpired over the last few decades (Al Shaer & Zaman, 2016; Marinova, Plantega & Remery, 2016; Dolamo, 2017; Lee-Hwei Khaw & Liao, 2018). The occurrence of these crises has encouraged a widespread belief that the absence of a highly effective board leads to poor firm performance and heightened management failures (Gompers, Ishii & Metrick, 2003).

Historical financial crises and corporate failures have included the stock market crash experienced by the US in 1929, the 1970s banking crisis in the UK, the 1980s loan crisis in the US and the Enron scandal that took place in 2001 (Ruparelia & Njuguna, 2016). These failures have not been restricted to developed nations but have also presented as a challenge in developing nations. Corporate governance failures are not unique; similar incidences occurred in sub-Saharan Africa, where more than 33 Kenyan banks failed in the 1980s (Barako, Hancock & Izan, 2006). South African examples include Masterbond, MacMedHealth Care, Fidentia, JCI, Randgold and Regal treasury (World Bank, 2003; Maroun & Cerbone, 2020). In recent times, corporate governance failures such as VBS and Steinhoff have attracted significant interest amongst academics and the general public (Naude, Hamilton, Ungerer, Malan & De Klerk, 2018; Rossouw & Stylian, 2019).

These failures have highlighted the need for more robust corporate governance mechanisms, hence the proliferation of various reforms. The UK has been the vanguard of global corporate

governance reforms (Ntim, 2015). In 1992, the Cadbury Committee issued the Cadbury Report, which provided recommendations on how boards should be structured as well as the responsibilities that boards should assume. The Higgs Report (2003), the Tyson Report (2003) and the UK Combined Code of Corporate Governance (2010), amongst others, subsequently followed. In the US, the financial scandals involving companies like Enron and WorldCom motivated the passing of the Sarbanes-Oxley Act on July 30, 2002 and later the Dodd-Frank Act in 2010 (Kostyuk, Mozghovyi & Govorun, 2017). Furthermore, the Securities Exchange Commission (SEC) was mandated with enforcing corporate governance law with the main provisions centred on addressing the structure and role of the board.

Contrary to the situation in other countries where the development of corporate governance codes was inspired by financial crises and corporate governance failures, South Africa's corporate governance frameworks were fomented by the need to strengthen global competition amongst its private sector (African Corporate Governance Network [ACGN], 2016). The necessity arose following the removal of economic sanctions that had been imposed by multiple nations in solidarity with the anti-apartheid movement (Armstrong, Segal & Davis, 2005). When South Africa issued the first King Report in 1994, it became the first developing nation to develop a corporate governance framework (Mangena & Chamisa, 2008).

The principles in the King I Report were inspired by many of the standards adopted in Commonwealth countries following the release of the Cadbury Report in the UK. According to Moloi (2009) as well as Moloi and Adelowotan (2019), the King I Report not only included financial and regulatory aspects, but had an all-inclusive approach to good governance that considered a wide range of stakeholders and promoted principles of good financial, social, ethical and environmental practice (Institute of Directors, 2002). Since then, three more reports have been issued, namely the King II Report (2002), King III Report (2009) and a recent fourth revision, the King IV Report of 2016 (Barac & Moloi, 2010; Moloi, 2009; Barac, Moloi & Marx 2011; Moloi, 2015). These efforts have led to the view that South Africa possesses one of the strongest corporate governance structures amongst emerging markets and African countries, where the efficiency of most corporate governance legal systems is considered weak (Abor & Fiador, 2013).

The structuring of boards is a recurring theme in the recommendations implicit within global corporate governance codes (Institute of Directors, 2016; UK Corporate Governance Code, 2018). The King IV Report provides recommendations on how firms should structure their boards for effective delivery of key board functions. These include recommendations on board sizes, board composition and various diversity elements. As part of the listing requirements,

firms listed on the JSE are required to apply the principles of the King IV report and explain any reasons for opting to deviate from the recommendations provided (Institute of Directors, 2016). This display of progression provides an interesting setting to study corporate governance related issues (Maroun & Cerbone, 2020).

A recent study by Bae, Ghoul, Guedhami and Zheng (2020) concluded that remodelling boards to adhere to sound corporate governance practices, strengthens the monitoring function of the board and simultaneously provides shareholders with strong rights to demand dividend payment from a firm's management. These results corroborate the dividend outcome model earlier suggested by La Porta et al. (2000) who advanced the view that dividend payouts were either an outcome or substitute for governance quality.

The agency theory views dividends as an effective monitoring tool for discouraging egocentric managers, while the resource dependence theories view aspects such as board diversity as qualities that enhance the board monitoring function and subsequently aid in reducing agency costs through diversity in cultures, perspectives and attributes. Against this background, this study used the agency and resource dependence theories to investigate whether dividends were an outcome or substitute of selected board characteristics of firms in the JSE Top 40. In other words, the study sought to establish whether a relationship exists between board characteristics and dividend payout.

1.3 PROBLEM STATEMENT

The global problem is the separation of ownership and control that encourages managers to make decisions suited for their best interests rather than for the benefit of shareholders, thus increasing agency costs (Jingura, 2018). Globally, many corporate scandals (Enron, Pollypeck, Maxwell, Parmalat) have taken place over the last three decades, leaving investors unsure of management capability to act as trustworthy stewards (BPP, 2015). Despite a well-recognised and sophisticated corporate governance framework, South African companies continue to experience challenges in maintaining well-balanced boards (Mans-Kemp & Viviers, 2017; Taljaard, Ward & Muller, 2015; Dolamo, 2017).

The Steinhoff case is an archetypal demonstration of poor corporate governance and the dangers of a poorly structured board (Rossouw & Styan, 2019). The failure of Steinhoff led analysts and academics to investigate the company's board structure and composition, with an interest in finding out whether the board was well suited to deal with agency problems and objective decision-making (Sewpersadh, 2019; Rossouw & Styan, 2019). Findings confirmed that Steinhoff, like many other South African companies, struggled with achieving an

independent board whose diversity reflected the demographics of the South African population (Naude et al., 2018).

Naude et al. (2018) identified weaknesses in the independence of Steinhoff's Non-Executive Directors (NEDs). Their concern was that the inclusion of family and friends in the Steinhoff board made it resemble the board of a family business (Naude et al., 2018). These concerns were heightened by declarations made by the Steinhoff's CEO at the time of the scandal, who referred to Steinhoff's board as 'a club of friendship and trust'. These sentiments raised questions on the extent to which the board was truly independent. However, it appears that Steinhoff's board diversity dynamics may have been the company's greatest governance challenge.

The King IV Code emphasises the need for the board to comprise the appropriate balance of knowledge, skill, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively (Institute of Directors, 2016). This concurs with the resource dependence theory, which emphasises the importance of diversity in corporate decision-making (Madhani, 2017). Unfortunately, this appears not to have been the case with the Steinhoff board.

Figure 1.1 below shows the ethnic and gender diversity of the Steinhoff board between 2009 and 2015.

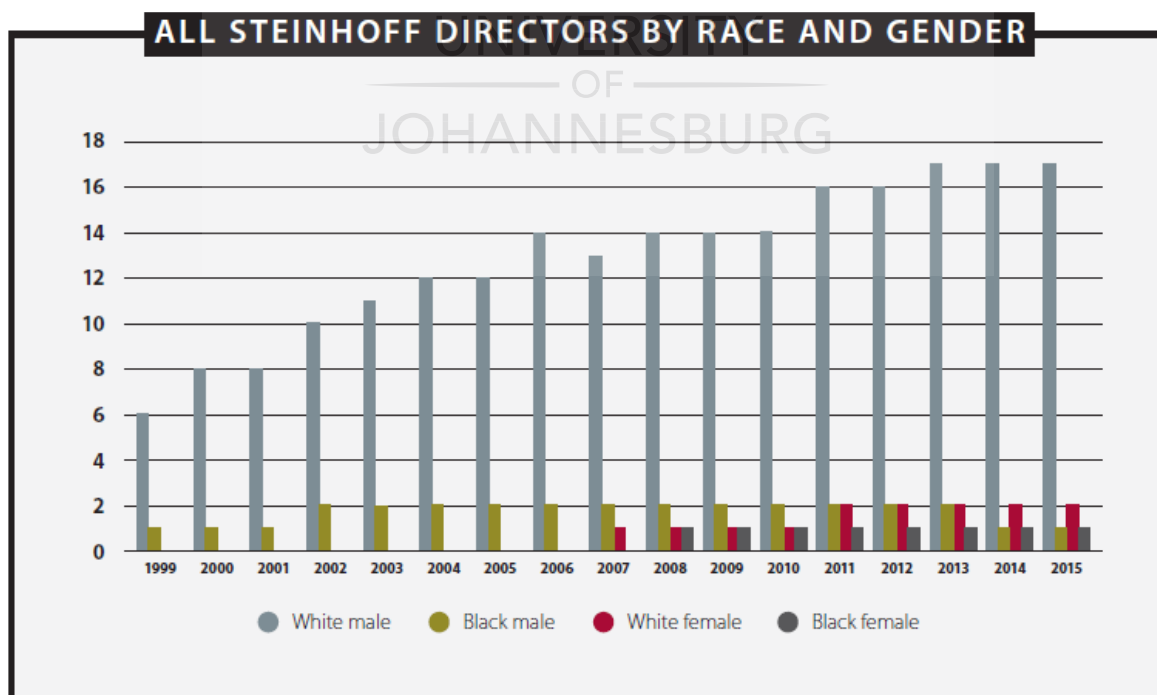


Figure 1.1: Ethnic and gender diversity in the Steinhoff Board

Source: Naude et al. (2018).

Figure 1.1 above indicates that between the years 1999 and 2015, white males dominated the Steinhoff board. This reflects a clear under-representation of women and the country's ethnic majority in the Steinhoff board. It is believed that the unique perspectives shared by a diverse board enhance decision making and improve monitoring. Hence, the lack of diversity in the Steinhoff board raises questions about its effectiveness in performing board functions, particularly in respect to monitoring and decision making.

It is interesting to note that in the four years leading to the Steinhoff scandal, the company's dividend per share increased by approximately 300%. The company's highest dividend appears to have been declared in the year before the scandal unfolded (IRESS, 2020). The question of whether high dividends were declared as an outcome of good governance or as a cover up to substitute for the poor governance and the brewing problems is a matter for further investigation.

A study by Goergen (2007) suggests mounting evidence that corporate governance mechanisms either substitute or complement each other and operate in tandem rather than in isolation. The board of directors is a mechanism that exists to address agency problems by endorsing, monitoring and controlling important decisions and various activities within an organisation. On the other hand, dividends play a role in reducing agency conflicts by minimising the amount of free cash flow available for managers to invest in projects suited for their own benefits at the expense of shareholders, thus inducing monitoring from external capital markets (Jensen & Meckling, 1976; Shamsabadi, Min & Chung, 2016).

It has been established that there is a relationship between corporate governance and dividend payout, but it remains unclear whether high dividends are an outcome of good governance or a substitute for corporate governance mechanisms. Unfortunately, previous studies have reached differing conclusions. A study by Elmagrhi, Collins, Crossley, Malagila, Fosu and Vu (2017) examined the relationship between corporate governance and dividend payout in UK listed Small to Medium Enterprises (SMEs). They found that UK SMEs with weak governance tended to pay higher dividends compared to firms with stronger governance. An American study by Atanossov and Mandel (2018) concurs with Elmagrhi et al. (2017), as results confirmed that weakly governed firms in their sample were more likely to pay higher dividends. These results support the substitute hypothesis.

Shamsabadi et al. (2016) found the relationship between corporate governance and dividend payout to be different for the Australian setting. Their results show that Australian firms use dividends as a monitoring device. In line with the outcome hypothesis, firms with strong

corporate governance paid high dividends. This is in line with the results of the study by Mans Kemp (2015) who found that the outcome hypothesis explained the relationship between corporate governance and dividend payout in South African companies. However, these results contrast with those of a study by Papo (2016) that revealed that South African firms with weak corporate governance substituted their failure to invest in lucrative projects by paying high dividends.

Previous South African research on the relationship between corporate governance and dividend payout has used structural corporate governance measures such as board size and composition. The limitation of this is that the broad effect of other corporate governance variables on the dividend payout decision remains uncaptured from a South African perspective. Additional variables such as race and gender diversity have been used to test relationships between corporate governance and financial performance in South African companies (Jonty & Mokoteli, 2015; Mans Kemp & Viviers, 2017; Taljaard et al, 2015; Taylor & Peens, 2017). However, their effect on various organisational outcomes such as dividend payout remains under-researched. The main contribution of this study to the existing body of knowledge is the introduction of a wider variety of variables, namely gender diversity, ethnic diversity, age diversity and financial expertise to studies examining the relationship between corporate governance and dividend payout.

Furthermore, a greater proportion of South African dividend decision studies have focused on the relationship between dividends and accounting-based variables such as leverage, profitability and firm size and have neglected to test the possible association between corporate governance and dividend decisions. This is despite the growing global interest in the relationship between corporate governance and corporate decisions. This study seeks to add to the dividends debate by extending literature to studies seeking to establish the determinants of dividend payout within a South African context.

1.4 RESEARCH QUESTION

The discussion above shows that existing South African studies examining the relationship between corporate governance and dividend decisions have used structural board variables such as board size and composition (Abor & Fiador, 2013; Mans Kemp, 2015; Papo, 2016). This study introduces demographic variables, namely gender diversity, ethnic diversity, the average age of the board and financial expertise, but also includes two structural variables, which are board size and board independence and two accounting variables, namely profitability and previous dividend as control variables.

Given the above, the main research question is;

- Could relationships between additional characteristics of boards of directors and the dividend payout in the Top 40 JSE Listed companies be established?

In order to address the central question, the following sub-questions were formulated, and they unpack the key research question on a step by step basis:

- Is there a relationship between board gender diversity and dividend payout?
- Is there a relationship between board ethnic diversity and dividend payout?
- Is there a relationship between the average age of the board and dividend payout?
- Is there a relationship between board financial expertise and dividend payout?

For control purposes, the following specific questions were posed:

- Is there a relationship between board size and dividend payout?
- Is there a relationship between board independence and dividend payout?
- Is there a relationship between the profitability of the company and dividend payout?
- Is there a relationship between previous dividend and current dividend payout?

1.5 RESEARCH OBJECTIVE

The main objective of this research was:

- To examine, through empirical evidence, the relationship between board characteristics and dividend payout of the top 40 South African companies on the JSE.

The study investigated the relationship between board characteristics (as represented by gender diversity, ethnic diversity, average age of the board, financial expertise, board size and board independence) and dividend payout in the top 40 JSE listed companies (dividend payout ratio).

1.6 PURPOSE OF THE STUDY

The purpose of this study was to ascertain the influence that selected board characteristics have on the level of dividends paid out by South African firms. On a broader level, the study adds to the existing body of knowledge on the determinants of dividend payout, whose results have been inconsistent in studies conducted between developed and developing economies (Fusire, 2018). The analysis conducted in this study is performed against the background of

the outcome and substitution hypothesis and will reveal the extent to which dividend payouts are used to reduce agency problems in South African firms.

The main contribution of this study to the body of knowledge is envisaged as the introduction of demographic diversity variables in a South African dividend decision study. The study is of great importance, given South Africa's unique political history of gender and racial inequality. The inclusion of these variables will inform investors, regulators and policymakers about the extent to which board diversity can improve monitoring effectiveness. Furthermore, this study will contribute to the debate on whether the South African government should consider implementing diversity quota legislations such as those implemented by Spain, Netherlands and France (Jonty & Mokoteli, 2015).

1.7 RESEARCH METHODOLOGY

1.7.1 Methodology

This study investigated the relationship between board characteristics and corporate dividend payout. In order to determine this relationship, a quantitative approach was used. A quantitative research paradigm is one in which the researcher collects data in a way that is easy to quantify and allows for statistical analysis (Patten & Newhart, 2017). Previous researchers have made use of quantitative research methods due to the quantifiable nature of the data and the need to link observations (Leedy & Ormrod, 2014).

The study followed an approach similar to the one outlined by Patten and Newhart (2017) who suggest that a quantitative research paradigm should involve the following:

- a review of literature;
- an identification of theories and empirical evidence that might assist in establishing the relationship with the case under study;
- a formulation of hypotheses to be tested;
- a plan for sampling and collecting data, and
- the statistical evaluation of the sample in question.

In line with similar research, this study used a simultaneous panel regression method (Gugler & Yurtoglu, 2003; Jiraporn, Kim & Kim, 2011; Abor & Fiador, 2013; Benjamin & Biswas 2019). According to Hsiao (2014), panel regression is an empirical model that measures both cross and time sections of data. The panel regression is an important tool for studies that span over a long period. This is because panel regression allows for a wider data file and is

accommodative to many observations (Hsiao, 2014). For the purposes of this research, the panel regression was chosen because of the need to statistically examine the relationship that exists between multiple board characteristics and dividend payout for a significant number of companies over a six-year period (2013 to 2018).

There are three types of panel data analysis techniques, namely the pooled ordinary least squares (OLS) model, the fixed effects model and the random effects model (Brooks, 2013). All three were considered in determining the most appropriate model for the study to account for the limitations inherent in each model. The merits of the pooled regression model lie in the assumption that the mean and variance are the same throughout all the variables. The fixed effects model takes into account the individual characteristics of the variables under consideration (Brooks, 2013). Similar to the fixed effects model, the random effects model accounts for heterogeneity, but slightly differs in its assumption that heterogeneity is not correlated with the independent variables. In the end, the pooled OLS regression was selected as the most suitable method.

The study used a non-probability convenience sampling method to select a sample for testing from the top 40 JSE listed South African companies. Convenience sampling was considered a viable option to facilitate proximity and accessibility of data during the period of study. As previously stated, use of the top 40 is considered an equitable reflection of the activities of the South African stock market (Courtney Capital, 2013). According to Kotze (2017), the Top 40 Index is perceived as a key market indicator because it captures 80% of the total market capitalisation of JSE listed shares and is designed to act as a performance indicator. In addition, the audited financial information of JSE listed companies is widely available.

First, the list of top 40 companies was extracted from the Equity RT Database. The Equity RT database is a global data management company that specialises in financial market research. From there, data was collected from publicly available audited annual reports for the years 2013 to 2018. Two types of data were collected for this study. Data relating to board characteristics of companies in the sample selected was manually extracted from their annual reports, which were sourced directly from their company websites. The financial variables, which consisted of the dependent variable (dividend payout) and two firm specific control variables (profitability and previous dividend), were collected from the IRESS database.

To determine the relationship between board characteristics and dividend payout, the study used the dividend payout ratio as the dependent variable and demographic board characteristics, board gender diversity, board ethnic diversity, average age of the board and

financial expertise were used as the main independent variables under study. The control variables included structural board characteristics, board size and board independence in addition to accounting based variables, namely profitability and previous dividend. Control variables are those factors which could have a possible influence on the dependent variable (Nestor & Schutt, 2018).

A more detailed discussion of the methodology followed is in Chapter 3 of this study.

1.7.2 Ethical considerations

It is expected that all researchers of the University of Johannesburg, both students and staff members apply for ethical clearance or exemptions for ethical clearance for all research conducted. In line with this requirement, this study applied for ethical clearance for research involving secondary data (no human participation).

The School of Accounting (SoA) at the University of Johannesburg, under which the present study falls, has a Research Ethics Committee (SAREC), whose main objective is to maintain the highest ethical standards of practice in research carried out under its jurisdiction. SAREC meets monthly to adjudicate on all submitted applications. This is carried out under the mandate of the College of Business and Economics (CBE). Accordingly, ethical clearance was obtained from the university in 2020.

The use of secondary data meant that all data was obtained from publicly available financial statements, which reduced the need to obtain consent from the companies involved. Furthermore, this eliminated any confidentiality threat.

1.8 LIMITATIONS

First, lack of access to a database containing the corporate governance variables meant that the data collection process was cumbersome. This had a major influence on the sampling strategy. In the end, the study's sample size was small. A larger sample size could have yielded different results.

Second, the sample was restricted to the top 40 companies of the JSE. This meant that smaller companies were overlooked in the process. It would be interesting to see how board characteristics affect dividend payout in SMEs.

Lastly, there are different measures of diversity, and the study could implement only some of them in this study. Implementing all could have yielded different results. Generally, the adjusted R squared (explanatory power) in studies using social elements (such as diversity) is low. However, exploring other measures of diversity could have assisted in building a statistical model with higher explanatory power.

1.9 CHAPTER OUTLINE

This research comprises six chapters as detailed in **Table 1.1** below.

TABLE 1.1: Summary of chapters

CHAPTER	CONTENT
Chapter 1:	Introduction and background to the study An orientation and motivation for the study is given in this chapter. Furthermore, the chapter explains the research problem.
Chapter 2	Literature review: An analysis of both theoretical and empirical literature relating to corporate governance is carried out in this chapter.
Chapter 3:	Literature review: An analysis of both theoretical and empirical literature relating to dividends is carried out in this chapter. In addition, the link between corporate governance and dividend payout is explored and research hypotheses are formulated.
Chapter 4:	Research methodology A discussion of the research design and methodology used in the study is given in this chapter.
Chapter 5:	Analysis of results In this chapter, the results of the study are discussed.
Chapter 6:	Discussion, conclusion and recommendations A conclusion based on the findings in chapter 5 is drawn to ascertain whether the research objective has been achieved. Limitations and recommendations for future research are also discussed.

Chapter 2 Literature Review – Corporate Governance

2.1 INTRODUCTION

The literature review of this study extends over two chapters, namely chapters 2 and 3. The goal of this review is to show the existence of research gaps in the extant literature on board characteristics and dividend payout. The study investigated the relationship between board characteristics and dividend payout. Hence, chapter 2 reviews corporate governance theories and codes addressing the structure and role of the board of directors. Chapter 3 is an extensive review of dividends, leading to the link between board characteristics and dividend payout policy and, finally, the research gaps and hypothesis.

Figure 2.1 below provides an overview of the discussions held in the study's literature review.

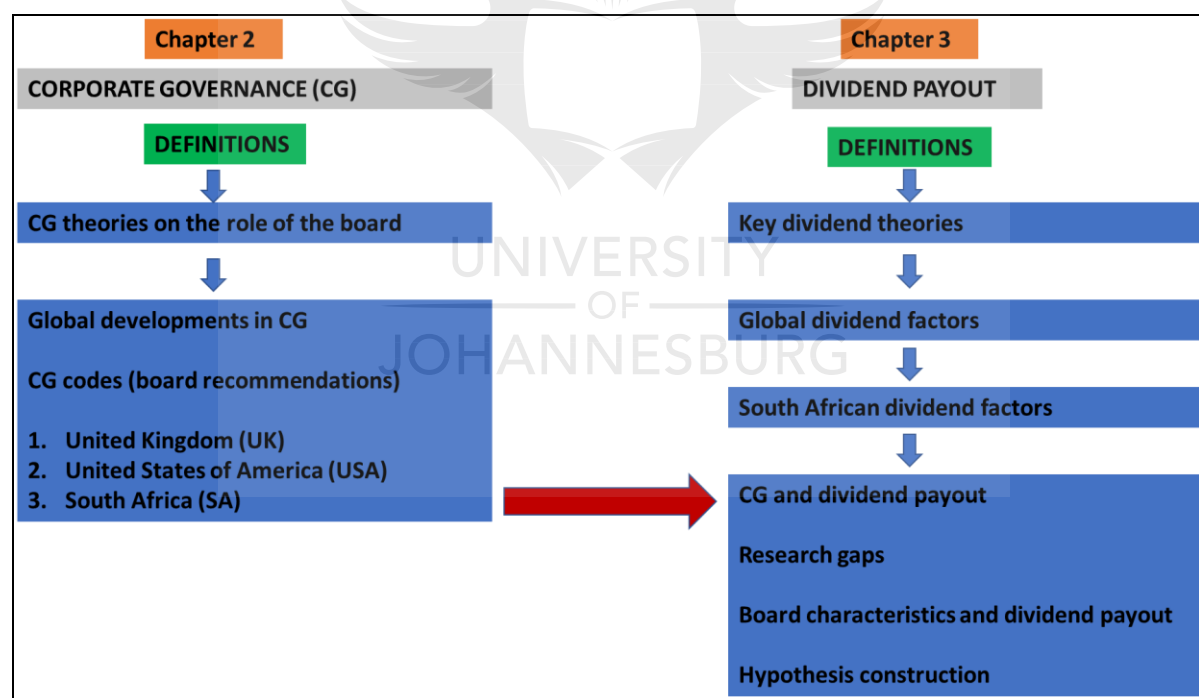


Figure 2.1: Literature review overview for this study

Source: Author's own construction

This chapter is structured following four distinct sections. Section 2.1 provides the introduction and contextual setting of the study. Section 2.2 provides several definitions of corporate governance and describes the role and attributes of the board of directors as outlined by

several corporate governance theories and codes of best practice. In addition, Section 2.3 reviews global and South African developments in corporate governance, whereas section 2.5 provides a summary of this chapter.

2.1.1 The Johannesburg Stock Exchange (JSE)

This section provides a brief overview of the setting of the study, which is the JSE. This is deemed important so that the results of this study are comparable to past or future studies conducted within a similar environment as well as to inform the applicability of the results.

According to Lukasiewicz (2019), the JSE is Africa's oldest surviving capital market. It is a platform enabling the free trade of securities under a regulated environment. The JSE functions not only to inject funds into the South African economy but also to reward investors with dividends when returns on investments are achieved.

Founded on 8 November 1887, the JSE developed into a renowned stock exchange, providing an alternative to the London and extant Southern African exchanges (Lukasiewicz, 2017). The history and development of the JSE is intertwined with the development of the gold mining industry in South Africa, embodying the country's economic, financial and political transformation. The increase in gold production in the Witwatersrand region in 1887 resulted in the increase of financial services providers but, more importantly, of the JSE (Lukasiewicz, 2019).

Alongside strong performances by the mining and agricultural sectors in the JSE's earlier years, South Africa witnessed a rapid increase in industrialisation and mass production. Mining houses ventured into production of goods to support mining activities. By the mid 1960's, manufacturing accounted for 30% of the Gross Domestic Product (GDP) (Lukasiewicz, 2019). The South African government encouraged industrialisation by extending tariff protection and establishing the Scientific and Industrial Research Council (HSRC) and the South African Bureau of Standards (SABS) (De Beer, Keyser & Van Der Merwe, 2015).

The number of industrial companies grew from 50 prior to World War II to about 348 by 1948, indicating the expanding range of secondary industries (De Beer et al., 2015). As of April 2020, there were approximately 400 companies listed on the JSE, varying across different industries and sectors (JSE, 2020). The mining industry is a mass employer and contributor of large export revenues through its support of a wide range of services and industries (Maroun &

Cerbone, 2020). Against this background, it remains the backbone of the South African economy.

According to De Beer et al. (2015), the period between 1960 and 1994 became a period of international isolation for South Africa and the JSE where investment was 'trapped' in South Africa. The implications were that many mining houses could not expand into international markets. However, the changes in South Africa's political dispensation in the 1990's marked South Africa's return to international markets. The JSE was included in the International Finance Corporations Investable (IFCI) emerging market index, which saw a dramatic increase in foreign participation. The increase in foreign participation gave rise to international discontent on the unfair racial treatment of black staff working for mining companies listed on the JSE (De Beer et al., 2015).

Increased criticism led to the restructuring of the JSE through adaption of international corporate governance structures as well as labour practices. Since then, the JSE has been a proponent of sound corporate governance practices (ACGN, 2016). In subsequent years, the JSE has had strong global influence following its listing requirements around the King Code of Corporate Governance and becoming the first stock exchange to foster the move towards an integrated reporting approach (ACGN, 2016).

Accordingly, the progressive stance taken by the JSE in adopting sound corporate governance practices makes South Africa an interesting setting for examining concepts around corporate governance (Maroun & Cerbone, 2020). This informed the focus of this study.

2.2 CORPORATE GOVERNANCE: A GLOBAL PERSPECTIVE

The study investigated the relationship between board characteristics and dividend payout. The board of directors bears the ultimate responsibility for corporate governance within an organisation and is relied upon by the shareholders to ensure that their interests are not jeopardised. Against this background, it is necessary to define corporate governance and review various corporate governance theories with a view to understand the wider role and characteristics envisaged for the board of directors. The next section defines corporate governance and describes the role and attributes of the board of directors as outlined by several corporate governance theories.

2.2.1 Definition of Corporate Governance

Despite various explanations of corporate governance, no single universal definition exists (Jingura, 2018). Therefore, corporate governance is often viewed from different angles, but with a seemingly common theme. The UK Committee on the Financial Aspects of Corporate Governance offers a modest interpretation, which defines corporate governance as ‘the system by which companies are directed and controlled’ (Cadbury Committee, 1992, p. 1). According to John and Senbert (1998, p. 372), ‘corporate governance deals with mechanisms by which stakeholders of a corporation exercise control over corporate insiders and management such that their interests are protected.’ Not very different from this, the Organisation for Economic Co-operation and Development (OECD) (2015) submits that ‘corporate governance includes a set of relationships between a company's management board, its shareholders and other stakeholders. Furthermore, corporate governance provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performances are determined.’

The King IV Report (2016) defines corporate governance as “the exercise of ethical and effective leadership by the governing body towards the achievement of specific government outcomes, namely ethical culture, good performance, effective control and legitimacy” (The Institute of Directors South Africa, 2016). From a legal perspective, corporate governance directs attention to the rules of capital markets focusing on investments in listed companies, namely listing requirements, insider dealings, disclosure and accounting and the protection of minority shareholder rights (Clarke, 2015).

Economies that have put significant efforts in developing efficient corporate governance systems have realised better performance outcomes (Bekaert & Harvey, 2002; Klapper & Love 2002). Those that have neglected the development of corporate governance regulations and systems have been susceptible to slow economic growth, increased costs of capital and have had more difficulty in securing equity investors (Clarke & Monkhouse, 1995; Klapper & Love 2002)

In recent years, many academics have examined corporate governance related topics due to its growing importance. The rise in corporate governance failures led to the development of systems and frameworks that govern an organisation's internal control and attempted to give assurance to investors that value and wealth were being created and maintained on their behalf (Clarke, 2015).

Earlier codes of corporate governance culminated in a worldwide effort to develop codes of best practice that suited their individual national needs (Brennan & Solomon, 2008). The widely held belief is that corporate governance is an important mechanism for the institutional development of global economies and a vital instrument for sustainable economic development, especially for emerging market economies (Clarke, 2015). Good corporate governance fosters a striking investment environment, which is critical for companies seeking to gain competitive advantage in efficient financial markets (Kayalvizhi & M Thenmozhi, 2018).

Corporate governance has its firm foundations on the agency theory, which deals with separation of ownership and control (Jensen & Meckling, 1976; Moloi, 2009; Moloi & Marwala 2020). The divorce of ownership from control is perceived to provide problems for some companies, and these include differences in priorities and information asymmetry between shareholders and managers (Moloi & Marwala 2020). This separation gives rise to opportunistic behaviour by managers who may make decisions that serve their own interests, excessively use capital and make inappropriate decisions (Panda & Leepsa, 2017). This opportunistic behaviour amongst managers increases risk and gives rise to certain asset maintenance costs termed 'agency costs'. The need to reduce these costs ushers in the need for controlling and monitoring mechanisms (Jensen & Meckling, 1976). Corporate governance serves as one of these mechanisms (Salehi, Sadatifar & Adibian, 2020).

The ultimate responsibility of ensuring good governance is entrusted to a company's board of directors (Jingura, 2018). The outcome of fine corporate governance rests in the hands of the board, which ensures that the interests of investors are not jeopardised (Madhani, 2017).

McNulty and Pettigrew (1999) classified the role of the board from three stand points; the board as a monitoring instrument, the board as a decision maker and the board as a link to the external environment for the acquisition of critical resources. Later on, Madhani (2017) identified four roles and responsibilities that are discharged to the board of directors, namely the control role, the strategic role, the service or resource provision role and, lastly, the advice and counsel role.

2.2.2 The role and responsibility of the board: Corporate governance theories

2.2.2.1 The agency theory

The agency theory perspective can be likened to McGregor's Theory 'X' (1960) perspective that takes a rather pessimistic view of human behaviour. In this view, McGregor posits that

humans are generally self-absorbed and uninterested in the needs of the company at large. McGregor's view shares a lot in common with the agency theory, which reflects management as self-serving individuals whose activities need to be coordinated and controlled (Oluwakayode, Clinton, Stanley & Subi, 2017).

Against the background of the agency theory, directors can be contextualised from the principal-agent relationship where agents are managers, principals are the owners, and the board is a crucial monitoring device (Jensen & Meckling, 1976; Madhani, 2017). The implication is that board-monitoring activity reduces the opportunity for managers to act in a self-serving manner at the expense of investors, thus lowering agency costs and increasing returns for the owners of a company (Madhani, 2017).

Although the agency theory identifies the monitoring role of the board, it can be argued that monitoring alone is insufficient to guarantee good corporate governance. Hence, a number of scholars have hypothesised various models that focus on other board functions (Madhani, 2017).

The role and impact of the board of directors from the perspective of the agency theory is provided in **Figure 2.2** below.

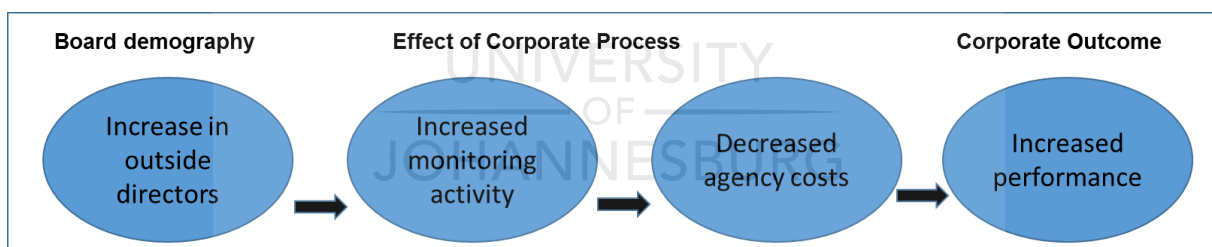


Figure 2.2: Agency theory perspective of the role and impact of the board of directors
Adapted from: Madhani (2017)

2.2.2.2 The stewardship theory

Another theory that explains the role of the board of directors is the stewardship theory. This theory of corporate governance can be likened to the Theory 'Y' of motivation (McGregor 1960), which displays confidence in human beings' ability to work independently and productively for the attainment of organisational objectives (Oluwakayode et al., 2017). The stewardship theory posits that excessive monitoring from the board is unnecessary for real impact on firm performance. Unlike its predecessor, the agency theory, it divorces from a focus

on control and conflict and directs attention to co-operation and collaboration (Sundaramuthy and Lewis, 2003).

The Stewardship theory is built on the premise of trustworthy directors who can be trusted to do a professional job, motivated by their inclination towards fairness, justice and an understanding for others. Hence, directors assume the role of company stewards. Under this theory, in order to protect their reputations, directors are unwilling to disadvantage shareholders (Donaldson & Davis, 1994). As stewards, directors will ensure that they act diligently in a non-self-serving manner to increase shareholders' wealth (Joslin, 2019). According to Joslin (2019), Japanese directors are known to display the loyalty explained by the stewardship theory through their heightened display of affection for the companies they work for. However, the key limitation of the stewardship theory is its inability to address circumstances where managers act as bad stewards (Madhani, 2017).

Figure 2.3 below depicts the role and impact of the board of directors from the perspective of the stewardship theory.

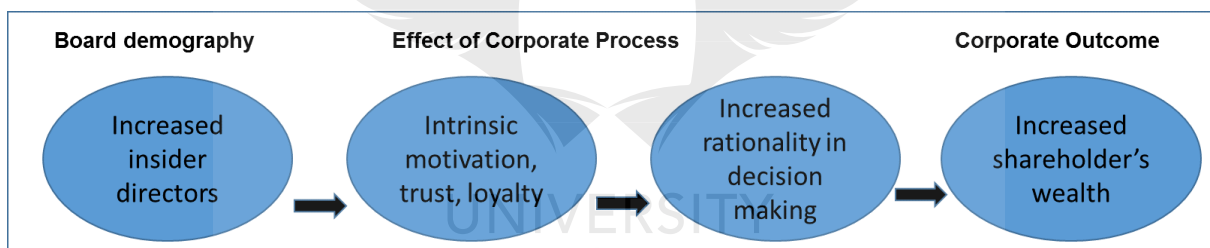


Figure 2.3: Stewardship theory perspective of the role and impact of the board of directors

Source: Author's own construction

2.2.2.3 The resource dependence theory

The role of the board can be viewed from the perspective of the resource dependence theory, which posits that the board serves as a link between a company and its external environment for access to critical resources (Madhani, 2017). The main focus of the resource dependence theory is the strategic actions of firms that control interdependencies with organisations in their ecosystem. In general, organisations do not have access to all the resources they need to function and will tend to rely on external resources. This creates the need for interdependencies. Therefore, companies ought to manage uncertainty as effectively as possible (Pfeffer & Salancic, 1978).

The role of the board under the resource dependence theory is to act as a mechanism for managing outside dependencies and uncertainties and reducing interdependency linked transaction costs (Pfeffer & Salancic, 1978; Williamson, 1984). According to the resource dependence theory, the extent to which the board achieves success in its governance determines the legitimacy of the board.

The resource dependence theory views board composition as a means to respond to external challenges faced by a firm (Hillman, Cannella & Paetzold, 2000). This is acknowledged in the King III report of corporate governance, which suggests that companies are able to source resources through appointing directors with the ‘appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively’ (Institute of Directors, 2009, p. 32).

The board must be composed in a manner that it provides expertise, advice and counsel, links the firm to crucial stakeholders, providing access to resources and aiding in strategy formulation (Hillman & Dalziel, 2003). A connected director is more likely to source and attract much needed resources for an organisation (Olowosegun & Moloi, 2020).

The role and impact of the board of directors from the perspective of the resource dependence theory is depicted in **Figure 2.4** below:

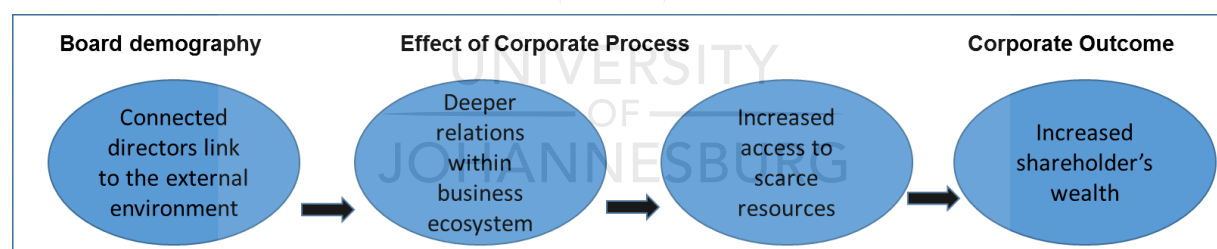


Figure 2.4: Resource dependence theory perspective of the role and impact of the board of directors

Adapted from: Madhani (2017)

2.2.2.4 The resource based view theory

According to the resource-based view, companies are characterised as packages of tangible and intangible resources (Penrose, 1959). These resources may translate into a sustainable competitive advantage if they are rare, inimitable and non-substitutable (Barney, 1991). This is similar to strategist Michael Porter's view that competitive advantage is obtained when a company's offering is unique and inimitable any competitive advantage becomes non-existent when offerings are replicated (Porter, 1985). This requirement for rare and unique resources

can be applied to unique board characteristics that are difficult to replicate such as its members' financial expertise and experience. This does not agree with the agency theory, which places greater significance on monitoring and control. Rather, the resource based view focuses on the role of the board in bringing unique resources to a company for the maximisation of shareholder wealth (Madhani, 2017).

According to Picincu (2020), a key limitation of the resource based view is its assumption that unique and valuable resources will translate into a competitive advantage. Competitors may yield results similar to a firm with unique resources (Picincu, 2020). It is then possible that a board with unique characteristics may fail to yield outstanding results if other important factors such as strategic planning and regulatory policies are not considered.

2.2.2.5 The stakeholder theory

Miles (2015) is of the view that the stakeholder theory is a combination of many theories and, as such it is subject to many interpretations from different subject fields. The major debate lies on who should be identified as a stakeholder (Miles, 2015). Various authors corroborate that stakeholders are those who are either effected or affected by a company's operations.

Various stakeholders provide the organisation with much needed resources, enjoy benefits from the organisation and influence its productivity (Donaldson & Preston, 1995). In other words, stakeholders are at the centre of value creation. It is therefore important for the board to take a more inclusive approach to corporate governance by considering the interests of all stakeholders. Under the stakeholder theory, the board plays the role of 'advocate' by catering for multiple constituencies that are affected by an organisation's activities.

In the Fourth Industrial Revolution (4IR), the company network of stakeholders is increasing as progressive organisations are no longer operating as single entities, but as members of a broader ecosystem. This view is supported by Moloi and Marwala (2020). Kaplan (2019) describes this ecosystem as a web of interdependent enterprises and relationships that create and allocate business value. According to the stakeholder theory, the board ought to act in favour of all stakeholder parties, whether internal or external (Arsad, Said, Yussuf & Ahmad, 2018).

Some researchers have criticised the stakeholder theory, indicating that it provides opportunistic managers with an excuse to make self-serving decisions under the premise that

they are of the benefit to other stakeholders (Phillips, Freeman & Wick, 2003). According to Sternberg (2000), the stakeholder theory dismantles business accountability

2.3 THE DEVELOPMENT OF CORPORATE GOVERNANCE

2.3.1 UK corporate governance

Corporate governance is not an entirely new concept. It can be traced back to Berle and Means (1932) who hypothesised that companies that progressed into very large modern corporations could develop a system of control divorced from ownership. The Cadbury Report (2002) acknowledges that the development of mechanisms aimed at controlling management actions have been intertwined with the growth of the corporation.

Financial crises in developed nations heightened the need for more robust corporate governance mechanisms. The South Sea bubble that took place in the 1700s motivated the introduction of new business laws and practices in England. Other financial crises that followed were the US 1929 market crash, the 1970s banking crisis in the UK and the 1980s loan crisis in the US (Ruparelia & Njunguna, 2016). The development of corporate governance codes gained prominence in the 1980s and 1990s due to the rise in corporate failures (Elmagrhi et al., 2017). In the UK, corporate governance reforms followed corporate failures such as Barron's Bank for Credit and Commerce International. These crises led to a widespread belief that effective management could only be achieved by an effective board (Gompers, Ishii & Metrick, 2003).

The development of UK corporate governance is rooted in the concept of stakeholder value which is very common in Anglo-American governance structures and also relates to the agency theory view (Pletz & Upson, 2019). The corporate governance structures and mechanisms employed in the UK share a lot in common with South African corporate governance systems. Hence, the next section is a discussion of the global developments in corporate governance with a stronger emphasis on developments in the UK. There are many aspects of corporate governance. However, against the background of the narrowed research focus to the board of directors, the next discussion reviews literature in corporate governance from the lenses of the board of directors.

2.3.1.1 The Cadbury Report (1991)

The Cadbury Committee issued the Cadbury Report in 1991, offering a number of recommendations aimed at strengthening accountability, responsibility and transparency of

managers in the board (Elmagrhi et al., 2017). The Cadbury Report included the following board recommendations:

- The power of decision should not be concentrated in one individual;
- A larger proportion of the board must be Non-Executive Directors (NED's);
- At least three NEDs must serve on the Audit Committee and NEDs must form the majority of membership for this committee, and
- The selection and engagement of board members ought to be delegated to the nomination committee consisting of at least one non-salaried director.

However, the appointment of directors is to remain a matter of concern to the whole board.

The Cadbury Report emphasised the financial and board composition aspects of corporate governance and neglected matters of equal importance such as executive and risk management practices (Ntim, 2015 a,b). These limitations led to the further development of other governance codes.

2.3.1.2 The high-level overview of the Greenbury Report (1995)

The Greenbury Report focused on improving corporate governance by ensuring a more cohesive link between executive pay and corporate performance. The report provided the following recommendations:

- Only non-salaried directors with no connection to the company should serve on the remuneration committee;
- The chairman of the leadership should attend the AGM to answer any questions on executive remuneration;
- There should be full disclosure of directors' remuneration in the annual reports;
- Directors should be placed on fixed-term contracts as a means to eradicate 'extensive' golden handshakes, and
- Directors' remuneration should be linked to performance to enhance lasting company performance.

2.3.1.3 The high-level overview of the Hampel Report (1998)

The Hampel Report agreed with a number of recommendations by the Cadbury and Greenbury reports. The Hampel Report took a firmer approach than that pursued by the Cadbury Committee. One major difference between the Greenbury Report and the Cadbury

Report lay in the Nomination Committee's recommendations. The Cadbury Report's proposal that NEDs should be selected through a formal process and remain a matter of the board had been viewed as only one approach and implied other possibilities (Cadbury Report, para 2.4). The Hampel Report went further to suggest that appointments by the Nomination Committee should be viewed rather as best practice than as one approach.

The Hampel Report suggested a 'lead' non-executive director to intervene where the roles of the chairman and chief executive were intertwined. Previously, the Cadbury Committee had been innovative in suggesting that a recognised senior member could intervene but did not stipulate whether the senior member of the board was to be an executive or independent director (Stapledon, 1998). The intention of the Hampel Report was to combine elements from the Greenbury Report and the Cadbury Report and extend further recommendations to form the UK Combined Code of Corporate Governance (Stapledon, 1998). This report was issued in 2003 and then revised in 2006, 2008 and 2009 to later form the basis of the UK Corporate Governance Code issued in 2010.

Afterwards, several other reports followed, providing new recommendations and addressing weaknesses in existing recommendations. The reports and codes are illustrated in **Table 2.1** below.

Code/Report	Year Introduced	Purpose	Revision dates
Turnbull Report	1999	Guidance for directors on good internal controls	2005 (Superseded by 2014 Financial Reporting Council Risk Guidance)
Myners Report	2001	Addressed institutional investors and established best practice for investment decision making in pension funds	-
Higgs Report	2003	Best practice on how to build a better board Focused on the role and effectiveness of NED's	Replaced by the FRC Guidance on Board Effectiveness in 2006.
Tyson Report	2003	Recommendations on diversity for effective boards	-
UK Stewardship Code	2010	Best practice for institutional investors to engage in good corporate governance	2012, 2020

UK Corporate Governance Code	2010	Initial focus on the accountability of the board. Later developed to strengthen other aspects such as sustainability and transparency	2012,2014,2016,2018
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Table 2.1: Summary of UK corporate governance codes and reports after 1998

Source: Author's own construction

2.3.1.4 The high-level overview of the Tyson Report (2003) and contributions to board diversity

As indicated in the table above, many corporate governance reforms followed after the Cadbury Report. The study views the Tyson Report (2003) as having offered significant contributions to the concept of board diversity. A revisit to the resource based view discussion alludes to board diversity as an important factor for the maximisation of investors' wealth. This is against the background that the rare and unique attributes of a board, which cannot be imitated, may lead to a sustainable competitive advantage for the organisation (Madhani, 2017). Against this backdrop, the Tyson Report (2003) followed up on the Higgs review of the role and effectiveness of NEDs.

The report's main focus was on the role of diversity through factors such as age, tenure, ethnicity, gender, qualifications and experience, on the effectiveness of the board. The Tyson Report (2003) aligned with and quoted an earlier study by Conger and Lawler (2001, p.11), which states that;

The best boards are composed of individuals with different skills, knowledge, information, power, and time to contribute. Given the diversity of expertise, information, and availability that is needed to understand and govern today's complex businesses, it is unrealistic to expect an individual director to be knowledgeable and informed about all phases of business. It is also unrealistic to expect individual directors to be available at all times and to influence all decisions. Thus, in staffing most boards, it is best to think of individuals contributing different pieces to the total picture that it takes to create an effective board.

The potential benefits of board diversity are tremendous, but there are challenges and costs that come with board diversity (Tyson Report, 2003). For example, companies may resort to selecting directors with insufficient qualifications and experience for the sake of their demographic characteristics. Furthermore, demographic dissimilarities may cause division and create conflict amongst board members (Ferreira, 2010).

The Tyson Report (2003) acknowledged the challenges inherent in board diversity and recommended a rigorous selection process for the appointment of NEDs. This process should include groups or talent that has been overlooked before and consider the needs and challenges of a company. Furthermore, the Report recommended extensive training for board members and emphasised that more diverse boards required more training to foster cohesion and trust amongst board members.

2.3.2 US corporate governance

Corporate governance in the US is often viewed as a paradigmatic setting of the shareholder approach to corporate governance. It is characterised by dispersed ownership, high engagement from institutional investors and small corporate boards with a high number of outsider directors for effective board processes (Aguilera, Williams, Conley & Rupp, 2006). Similar to the UK, corporate scandals were a huge motivation for the development of corporate governance reforms in America (Holmstrom & Kaplan, 2003). The Enron and WorldCom Scandals brought a lot of attention and criticism on US corporate governance.

According to Thomas (2002), several weaknesses became apparent and differences between governance structures began to show. The Enron Board displayed untrustworthiness in its disclosure of financial statements despite having fourteen outside members, with only two inside members (Li, 2010). Loopholes in accounting regulations allowed Enron to manipulate financial statements by giving investors a false picture that Enron was in a lucrative position. This manipulation resulted in the escalation of Enron price shares. The discovery of accounting fraud led to the fall in share prices, which declined from \$90.75 at its highest to \$0.26 at bankruptcy (Segal, 2020).

Following the Enron Scandal, the Sarbanes Oxley Act (SOX) was introduced in 2002 and became legally binding under the mandate of the Securities Exchange Commission. The main aim of SOX was to create legislation that protected investors and the public at large from unscrupulous practices of corporations. In addition, SOX sought to increase transparency in financial statements issued by corporations and sanctioned legislative guidelines to protect the public from erroneous and unethical business practices by American firms. It is also intended to increase transparency in financial reporting and strengthen audit practices within business entities (SOX, 2002).

The US Subprime crisis and the effects of the great recession that followed motivated the introduction of the Dodd-Frank Act in 2010. The Dodd-Frank Act had a number of

requirements on remuneration disclosure. Zalewska (2014) summarised some of the requirements as follows:

- Disclosure of information pertaining to executive remuneration and a justification of remuneration based on performance evidence;
- Disclosure of the ratio of the average total workforce compensation to the total compensation of the Chief Executive Officer (CEO);
- Disclosure on whether a company permits its directors and employees to buy financial instruments that hedge against a decline in the company's shares held by them as part of their pay package, and
- Request for the SEC to place a legal requirement on firms to explain their reasons behind their board structure, especially where there is CEO duality.

From the discussions above, it can be noted that a major difference between the UK and US corporate governance frameworks lies in enforceability. UK corporate governance codes are recommendations and proposals which companies can choose to 'comply or explain' while the US corporate governance system is legally enforceable and the matters raised, in the SOX for example, are legal requirements attracting fines and penalties for non-compliance.

2.3.3 The high-level overview of corporate governance in South Africa

As alluded to earlier, South Africa's economic history is intertwined with the growth of the mining industry. In earlier years, the success of the mining industry was largely due to the low costs of production that were achieved from the exploitation of black migrant workers (Wilson, 2001). Crush, Jeeves and Yudelman (1991, p. 1) wrote that 'there is little doubt that if large numbers of low-wage and skilled migrant had not been recruited from throughout the sub-continent there would never have been a deep-level gold mining industry in South Africa'. In addition to this, the mining houses were supported by colonial and apartheid policies.

The international community was appalled by the apartheid system and, triggered by the Rubicon speech, responded by placing economic sanctions on South Africa. This move signalled the beginning of South Africa's isolation years (De Beer et al., 2015). During this period, there was little to no foreign direct investment and the economy was crippled. A lack of interaction with international markets resulted in South African corporate governance practices and regulatory systems being a far cry from international standards (Malherbe and Segal, 2001).

Foreign participants who had re-entered the economy following South Africa's re-admission into the global economy were very critical of the systems and structures in place (De Beer et

al., 2015). A need arose for South Africa to foster credibility amongst international markets. Subsequently, this motivated the development of corporate governance in South Africa (ACGN, 2016.) According to Armstrong et al. (2005), the development of South Africa's corporate governance framework was motivated by the need to restore global competitiveness in South Africa. This is unlike the situation in developed countries where the development of corporate governance frameworks was inspired by corporate failures and financial crises.

South Africa's corporate governance has developed in line with the Anglo-American approach because of its colonial ties with Britain. The Companies Act, which came into effect in 1973 was influenced by the English Companies Act of 1908 (Maroun & Cerbone, 2020). The South African corporate governance framework comprises four main elements, namely common law, acts of parliament, standards, codes and guidelines and JSE listing requirements for companies with shares (ACGN, 2016).

2.3.3.1 King I Report

The first response to the need for sound corporate governance practices was the issuance of the King I Report in late November 1994. Most emerging countries form their corporate governance codes from established codes in developed countries (Samaha, Dahawy, Hussainey & Stapleton, 2012). King I was modelled on the Cadbury Report, which had been issued earlier in 1992 (Institute of Directors South Africa, 1994). The contributions of the King Report were significant in educating the South African public on the meaning of sound corporate governance practice (ACGN, 2016). However, King I was not a replica of the Cadbury Report; it went beyond the focus of the Cadbury Report by encouraging an inclusive approach of doing business (ACGN, 2016).

The proposals made by King I directed its attention to six broad areas, namely the board of directors, auditors, stakeholders, corporate reporting, ethics and compliance (Maroun & Cerbone, 2020). King I emphasised the importance of an effective board of directors as fundamental aspect of sound governance (Maroun & Cerbone, 2020).

In line with the 1992 Cadbury Report, King I proposed that South African companies should be headed by a single board that comprised a mixture of executive and NEDs. It placed the responsibility of directing and controlling the company on the board of directors. Furthermore, it required that all directors be accountable for maximising shareholders' wealth with regards to profits, cash flows and risk management (Institute of Directors South Africa, 1994).

Against the backdrop of the Cadbury Report, King I proposed that there be a separation between the duties of a CEO and a Chairman as a means to ensure that power was not over concentrated in one individual.

King I acknowledged the importance of NEDs in delivering effective corporate governance. It emphasised the contribution of board independence and appropriate skills and experience of NEDs to the company's strategy formulation, performance, allocation and acquisition of resources, and it directed that the appointment of board members be a matter of the whole board. Furthermore, the King I Report recommended that at least two NEDs serve on the board.

Other board recommendations of the King I Report were as follows:

- Every board should have remuneration and audit committees, and at least 2 members should be NEDs;
- Board members should undergo induction training on the company's business and organisational studies, and
- The recruitment and appointment of board members must be a matter for the whole board.

According to Tshipa (2017), the King I Report had the following weaknesses:

- Failure to acknowledge the importance of subcommittees (No recommendation was provided for the creation of a Nomination Committee);
- The inability to recommend a truly NED to chair South African boards;
- Failure to provide guidance on the level of a director's remuneration, and
- Failure to provide guidance on how to clearly distinguish the makings of an NED.

2.3.3.2 King II Report

In 2002, a second Corporate Governance Code was issued: King II. King II intended to improve a number of stakeholder related disclosures and in that regard, insisted on an inclusive corporate governance approach. It was specific in its requirement for companies to disclose their contribution towards Black Economic Empowerment, HIV/AIDS and the conservation of the environment (Gyapong & Afrifa, 2019). Similar to King I, King II was not directly legally enforceable as it applied the 'comply or explain' rule. However, it included all JSE listed companies and was explicit on which public sector entities should apply the code.

King II built up on the principles of King I and significant improvements were incorporated into the report (Tshipa, 2017). Its discussions included the board of directors, directors,

remuneration, internal control and risk management, accounting and audit. King II included the features below on its recommendations on the board of directors.

- King II recommended that a company's board should mostly consist of NEDs, a change from King I's recommendation of two NEDs. Furthermore, it recommended that the majority of the board should be independent non-executive directors.
- Similar to King I, King II encouraged the formation of diverse boards in terms of skills and demographics such as age, race and gender.
- One of the weaknesses of King I was that it did not specify whether the chairman of the board was to be an executive or NED (Tshipa, 2017). King II specified that the board should be chaired by an independent NED. It suggested the creation of a nomination committee. King I had only proposed the creation of the Audit and Remuneration Committee.
- An annual review of all board members' performance was recommended and clear guidelines were given to distinguish between executive, non-executive and independent non-executive directors. King II provided more clarity on the matter of executive remuneration, especially in respect to the level of packages. The general recommendation was that the remuneration package was to be sufficient to attract, retain and motivate the board of directors. However, to align the directors' interests to those of shareholders', performance-based remuneration was to form the bulk of the pay package. Furthermore, King II requested that all forms of remuneration including share options were to be fully disclosed.
- Lastly, King II advocated that directors, officers and other selected employees should be prohibited from dealing shares for a specified period prior to the release of the annual financial statements for any price sensitive information.

2.3.3.3 King III Report

A third revision of the King Code (King III) was released in 2009. In line with earlier codes, King III emphasised an inclusive approach to corporate governance. An important undertaking of the King III was the need to strike a balance between international corporate governance practices and African anomalies (Gstraunthaler, 2010). Unlike the previous King Codes which had adopted a 'comply or explain' approach, King III adopted the 'apply or explain' approach.

According to Jingura (2018), King III focused its attention on integrated reporting. Against this background, South Africa became the first nation to insist on an integrated report instead of an annual financial and sustainability report. King III required all companies choosing not to adopt this approach to provide an explanation of why they were opting not to (King III

Corporate Governance Code, 2009). The philosophy of King III lay in three main elements, namely effective leadership, sustainability and corporate citizenship (Maroun & Ceborne, 2020).

2.3.3.4 King IV Report

Like many other countries worldwide, South Africa is still grappling with inequality, high population growth and socio-economic challenges (Institute of Directors, 2016). The King IV Report was issued as a response to the political, economic and social challenges and the impact these challenges could have on the sustainable development agenda (Maroun & Cerborne, 2020). It outlines good corporate governance as an outcome-based exercise of ethical and effective leadership, seeking to achieve good performance, ethical culture, effective control and legitimacy (Institute of Directors, 2016).

King IV shifts from the 'apply or explain' approach that was introduced by the King III in 2009 to the 'apply and explain' approach. Under this approach, applying the corporate governance principles is expected of all entities. Furthermore, all entities should provide an explanation of how entities adopted the recommendations provided for by King IV.

With respect to board diversity, King IV emphasises that the board should have the appropriate mix of skills, knowledge and experience (both commercial and industry) needed to govern an organisation. This is in line with previous corporate governance codes. However, King IV goes further to advocate that instead of merely aiming to strive for a balance in diversity, entities should embrace gender and ethnic diversity targets in determining the number of board members.

The King Codes of Corporate Governance have evolved and continued to make improvements on the recommendations they provide. The overall picture emerging of South African corporate governance is that the country has maintained 'a sophisticated, legal, regulatory and corporate governance system' (Clarke, 2015). However, even with commendable codes of governance, South Africa has experienced several corporate scandals since the release of the first King Code in 1994 (Jingura, 2018; Maroun & Cerbone, 2020).

The list of scandals since 1994 includes Beige Holdings Limited, Johannesburg Consolidated Investments (JCI), Macmed, Saambou Holdings Limited, Tigon Limited, LeisureNet, Steinhoff and the State Capture that included entities such as KPMG, McKinsey, Naspers, SAP, Transnet and Eskom (Jingura, 2018).

2.4 SUMMARY

This chapter defined corporate governance and outlined the role of the board of directors as described in several corporate governance theories (the control role, the strategic role, the service or resource provision role and the counsel role). Furthermore, the global developments in corporate governance were discussed with the main focus on UK, USA and South African corporate governance. The various recommendations on the board of directors implicit in corporate governance codes were reviewed. It was established that the manner in which boards are structured plays a huge role in decision making and various organisational outcomes. The next chapter is an extension of the literature review, providing a link between corporate governance and dividend payout.



Chapter 3 Literature Review - Dividends

3.1 INTRODUCTION

Chapter 2 was a review of corporate governance related literature and major theories around corporate governance. Chapter 3 extends the literature by reviewing dividends and establishing a theoretical and empirical link between dividends and corporate governance. The main aim of this chapter is to uncover the research gap through an extensive examination of the extant literature.

Sections 3.2 and 3.3 provide a definition and brief global history of dividends. Section 3.4 is a discussion of the various theories that have formed the basis of global dividend literature and sections 3.5 and 3.6 review empirical literature on factors that determine global and South African dividends. In addition, section 3.7 is a review of empirical literature on corporate governance and dividend payout. The research gaps within the literature are outlined in section 3.8. Section 3.9 discusses the literature on board characteristics and dividend payout and formulates the research hypotheses. The conceptual framework of the study is presented in section 3.10. Finally, the chapter is summarised in section 3.11.

3.2 DEFINING DIVIDENDS

Managers make three fundamental 'corporate finance' decisions for the attainment of the organisation's strategic objectives. One of the decisions is to allocate financial resources to identified projects or investments that maximise the wealth of shareholders. In addition, they must make decisions on the most appropriate types and sources of funding for an organisation's investment and operational needs. Where sufficient profits are made, a third decision to distribute earnings to equity owners may be taken (Kaplan, 2019, p. 111 -114).

Hillier, Clacher, Jordan, Ross, Westerfield and Jordan (2017) refer to dividends as cash or shares issued out to a firm's owners as payment from earnings. Successful companies use earnings to invest in operating assets, acquire securities or retire debt, or opt to distribute earnings to equity owners. This earnings distribution to equity owners is known as dividend (Amidu & Abor, 2006). Ultimately, the dividend decision involves two central questions. Should the firm distribute earnings to its shareholders, or should some of them be retained to support

the growth of the firm? The dividend decision is therefore an important one, which may affect the value of the company (Hillier et al., 2017).

The term 'dividend payment policy' refers to "the practice that management follows in making dividend payout decisions or, in other words, the pattern of cash distributions over time to shareholders" (Firer, Gilbert & Maytham, 2008). According to Fusire (2018), the dividend payout decision refers to the level of earnings or how much of earnings will be declared as a dividend. In essence, dividend payout is a subset of dividend policy.

There are two kinds of dividend policy: managed and residual. In a managed dividend policy, management aims to achieve a fixed pattern of payments. A residual dividend policy involves distributing dividends only after capital expenditures on investments have been met. In other words, management issues out dividends to shareholders based on the residual or remaining earnings after obligations have been met (Murtaza, Iqbal, Ullah, Rasheed & Basit, 2018). This study examines the relationship between board characteristics and the level of dividends paid out (by use of the dividend payout ratio).

Once the decision on the pattern of payments has been determined, a further decision must be made on the method of payout. Organisations can pay various types of dividends to its shareholders. Dividends are often paid out in the form of cash but can also be paid out in the form of share dividends, share splits and share repurchases (Murtaza et al., 2018). Each of these methods will have their own advantages and disadvantages. For example, although cash dividends are common, they have the potential to effect negatively on both a company's liquidity and reserves. Hence, firms will assess their own specific circumstances before deciding on the method of payout.

Before the 1980's, firms in developed countries utilised cash dividends as the main method of distributing earnings to shareholders. Today, share repurchases have gained popularity as an alternative method of distributing cash. The increase in popularity can be attributed to the flexibility that share repurchases have over a scheduled dividend payments (Baker & Weigand, 2015). In addition, investors may choose capital gains obtained through share repurchases compared to dividend payments due to dividend income tax being higher than capital gains tax in most countries (Clayman, Fridson & Troughton, 2012). For the purposes of this study, the dividends referred to are cash dividends.

3.3 GLOBAL DIVIDEND DISTRIBUTIONS

The origins of dividends are pinned to Holland and Great Britain in the early sixteenth century where sea captains began to sell financial claims to investors. The investors obtained rights to a share of any proceeds made during a voyage. The end of each journey was characterised by the distribution of both capital and profit to investors. As the seventeenth century approached, these financial claims were openly traded on Amsterdam markets and were slowly replaced by share ownership. Investors spread out their risk by purchasing shares from more than one captain (Murtaza et al., 2018).

The distribution of profits at the end of each voyage forced sea captains to be accountable by reducing opportunities for fraud (Baskin, 1988). However, distributing both profits and capital became more complicated and costly as the profitability of these voyages became more regular. Shareholders gained more confidence in management (captains) as management paid out more 'generous dividends'. Eventually, companies began operating as going concern entities that distributed profit rather than the invested share capital. As firms adopted business as a 'going concern', the practice of distributing a portion of the firm's earnings became common and the first dividend regulations were drafted (Frankfurter & Wood, 1997).

As time passed, managers understood the importance of 'generous' and stable dividend payments in keeping investors satisfied. In the earlier stages of corporate history, government bonds were an alternative financial security that paid out stable and consistent dividends. Managers realised that investors preferred shares whose performance resembled bonds (Frankfurter & Wood, 1997).

Early in the 19th century, dividends were perceived as an important information tool. Investors made investment decisions based on a company's dividend payments due to the lack of reliable financial data. They used dividend policy as a means to detect management's view on future firm performance. Consequently, increasing dividend payments seemed to be reflected in high share prices and hence managers could use dividends to signal positive earnings prospects. Initially, it was perceived that as financial markets improved due to increased efficiency and accuracy of corporate reporting, dividends would cease to be an important factor in measuring firm value. Hence, the importance of dividend policy has been widely controversial (Al Malkawi, Rafferty & Pillai, 2010).

Dividends have emerged as one of the most debated areas of study in the area of corporate finance. Finance scholars have attempted to solve a wide range of matters relating to

dividends by framing theories and models to elucidate corporate dividend behaviour and yet there is no consensus around this subject. Hence, Black (1976) termed dividend policy a 'puzzle'.

3.4 DIVIDEND THEORIES

Lintner (1956) initiated the dividend debate when he carried out a series of interviews with managers in an attempt to explain factors that corporate managers considered when making dividend payout decisions. In addition, the interviews sought to identify management views on the impact of dividend policy on the value of the firm. Lintner (1956) established that managers made dividend decisions based on current year earnings and prior year dividends by setting long-term target dividend payout ratios. The study concluded that managers 'smoothed' dividends to avoid short-term effects of temporary earnings on dividend payments. Lintner (1956) found that 'corporate managers considered dividends a reflection of growth sustainability', hence impacting the value of the firm (Nyere & Wesson, 2019).

Since Lintner's (1956) seminal work, several theories have been formulated in an attempt to explain dividend behaviour. Three opposing dividend theories have been identified in literature. Some scholars argue that higher dividend payouts result in the increase of a firm's value while others hold the opposite to be true, suggesting that high dividend payouts have an adverse effect on firm value. The third view asserts the irrelevance of dividend payments, suggesting that any efforts directed to the dividend decision are wasted.

In this section, a number of theories are discussed, illustrating the views held on the relevance, or lack thereof, of dividends. The discussion in this section is not intended to address all known dividend theories and is by no means an exhaustive list of theories. However, a focus on the most documented theories has been maintained.

3.4.1 Dividend Irrelevance

Graham and Dodd (1934) posit that the only purpose for the existence of corporations is to distribute dividends, and hence the payment of dividends is relevant to the value of the firm. For this reason, their belief was that high dividend paying firms were justified in selling shares at premium prices. However, in a diverging view, Miller and Modigliani (1961) put forward a new proposition which suggested that under perfect capital markets, dividends are not relevant in determining firm value.

Miller and Modigliani (1961) demonstrated that the dividend decision is not exclusive in determining firm value. They purported that investors were unconcerned about whether they received dividends or generated capital gains. They suggested that the reason for this indifference is that the value of the firm is affected by the investment decisions that generate earnings rather than the distribution of earnings. In other words, investors determine firm value based on the value of future earnings, which are not influenced by how firms set their dividend policies.

Miller and Modigliani (1961) based their proposition on the assumptions of perfect capital markets and the rationality of investors. The assumptions they made for the irrelevance of dividends were that in perfect capital markets (1) all traders have equal and complete access to information about share prices; (2) there are no costs such as taxes and transaction fees when shares are traded; (3) there are no agency costs, hence, all investors are assured of future investment decisions and profits. After considering these perfect capital markets assumptions, Miller and Modigliani (1961) concluded that a company's investment decisions are the key determinant of value through positive net present value, while dividend policy is the residual.

Black and Scholes (1974) investigated the relationship between dividend yield and share returns to determine the impact of dividend policy on the value of the firm. Their results were consistent with those of Miller and Modigliani (1961). Their study concluded that neither a high nor low dividend yield had an impact on share prices; hence, it is in line with the dividend irrelevance theory.

3.4.2 Bird in the hand

Miller and Modigliani's (1961) hypothesis was based on perfect capital market assumptions that ignored the real world reality of uncertainty and less than perfect information. The implication of an imperfect market is that dividends will carry a value different to capital gains contrary to the suggestion of the irrelevance theory (Ang & Ciccone, 2009). This difference causes investors to prefer dividends in the present, rather than possible capital gains in the future. In other words, a 'bird in the hand' (cash dividend now) is better than 'two in the mind' (future capital gains).

This theory by Gordon (1959) was formulated on the premise that dividend paying shares are less riskier than non-dividend paying shares. Hence, Gordon (1959) posits that a firm that

pays dividends eliminates the risk associated with uncertain cash flows, causing the value of that share to increase. Gordon's (1959) view agrees with that of Lintner (1956) who had earlier on expressed that dividends were relevant in increasing firm value hence managers sought to pay consistent dividends. This is also in line with the views of Graham and Dodd (1934) who hypothesised that dividends had an impact on the value of the firm.

Later on, Bhattacharya (1979) contradicted Gordon's claims that non-payment of dividends increases the risk embedded in a company's share. Bhattacharya (1979) argues that it is the firm's risk that influences the level of dividend and not the other way round as suggested by Gordon (1959).

3.4.3 Investor sentiment and catering

Baker and Wurgler (2004) proposed a relatively new explanation: 'the catering theory of dividends.' They posited that investors' sentiment on the payment of dividends will vary over time. Their view was that investors may opt for a lower risk, dividend paying share in seasons of economic recession and prefer riskier shares that reinvest earnings instead of distributing them in boom seasons (Baker & Wurgler, 2004b). Hence, managers were prone to cater to the changes in investor's preferences over time by issuing or withholding dividends based on investor sentiments (Al-Najar & Kilincarslan, 2018)

By suggesting that dividends are relevant to the firm albeit in different directions over varying seasons, this theory provides a contrast to Miller and Modigliani's (1961) irrelevance proposition. A further investigation by De Angelo et al. (2006) and Denis and Osobov (2008) found evidence contradicting the 'catering' hypothesis. These researchers insist that investor sentiment does not explain the varying levels of dividends over time.

3.4.4 Taxes and clientele

Miller and Modigliani's (1961) irrelevance hypothesis was formulated under the assumption of a tax and transaction cost free capital market. In the real world, market imperfections such as transaction costs and differential income taxes could shape investors' preference between dividends and capital gains. Black (1971, p. 457) suggests that a rational investor 'will buy a well-diversified portfolio and hold on to it. He will generally sell only to establish tax losses, or when he needs money, instead of selling, to avoid realising capital gains. He will minimise investment expenses, brokerage costs and taxes'. From this, one can derive Black's (1971) attempt to demonstrate that in the real world, taxes and transaction costs are key determinants

in shaping investors' preferences between dividends and capital gains. This view was shared by Bhattacharya (1979) who strongly disagreed with Miller and Modigliani's irrelevance stance.

It is common practice in many developed countries for dividend income to be taxed at a significantly higher rate than capital gains (Nyere & Wesson, 2019). Generally, investors are concerned with the net return after tax deductions and hence are more inclined to choose the option with higher net earnings. The tax preference theory suggests that manager may prefer to lower dividends in an attempt to increase shareholders' wealth. The tax-effect hypothesis therefore suggests that the tax advantages associated with capital gains are favourable to investors who favour the tax treatment on capital gains; hence, investors are more willing to pay higher prices for companies with lower dividend payout (Bhattacharya, 1979). This view is in contrast with the bird in the hand theory and challenges the notion that dividends are irrelevant to firm value.

3.4.5 Signalling

Under Miller and Modigliani's (1961) perfect capital markets, all participants have equal access to the same information about a firm. Therefore, dividend payments have no effect on firm value. In actual markets, there is no perfect information asymmetry. This study revisits Lintner's (1956) model, which suggests that managers prefer to set long-term target dividend ratios and avoid any short-term changes. This model implies that dividends act as a signalling tool that conveys messages about future firm value to investors.

According to Firer, Gilbert and Maythan (2008), the signalling theory has its fundamental roots on the ideology that investors have less access to information when compared to managers and even if both managers and investors are privy to the same information, they will not perceive it in the same manner. The signalling theory suggests that managers will always try and act in the best interests of shareholders. Hence, shareholders will have to decide on the credibility of the information.

Baru (2019) posits that the signalling hypothesis is correctly used when certain conditions are met; for example, information provided by managers must be unique and paint an accurate representation of the firm's status quo. An increase in dividends can be perceived as positive news about a firm's future, whereas a decrease can be received as negative news about the firm. This may explain why managers are reluctant to decrease dividends (Lintner, 1956).

3.4.6 Firm life cycle

Various empirical studies examine the relationship that exists between dividend payout policy and a firm's lifecycle. This is often referred to as the 'maturity hypothesis'. Grullon, Michaely and Swaminathan (2002) postulate that firms that increase dividend payments realise declines in profitability in future, while those that reduce dividend payments will likely experience increases in profitability in future. They further submit that firms that have exhausted all investment opportunities are more likely to respond by issuing out more dividends. Thus, as firms transition from a growth phase to one of maturity, they are more likely to pay dividends of a larger size (Grullon et al., 2002).

De Angelo et al. (2006) and Denis and Osobov (2008) have results that are supportive of the life-cycle theory. Various researchers support this theory, which to a large extent nullifies earlier theories that attempted to explain dividends as mechanisms that reduced the negative effects of information asymmetries, as information asymmetry problems are less prevalent in mature firms.

3.4.7 Agency costs and free cash flow

Jensen and Meckling (1976) propose the agency cost theory. They define the agency relationship as one in which a party (the principal) appoints another (the agent) to carry out services on their behalf. In carrying out the principal's duties, the agent is granted decision-making authority. The greatest challenge in this relationship is ensuring that the agent acts in the best interest of the principal (McColgan, 2001).

The differing interests between management and shareholders lead to agency conflict. Managers seek out high remuneration while shareholders are more concerned with increased returns on their investment (Murtaza et al., 2018). 'Agency costs can be seen as the value loss to shareholders, arising from divergences of interests between shareholders and corporate managers' (McColgan, 2001, p. 4). Financial markets will factor in any captured agency problems into a company's share price.

According to Jensen and Meckling (1976), one of the areas in which agency conflict can occur is earnings retention. In another study, Jensen (1986) suggests that in the absence of lucrative positive NPV projects, managers are more inclined to retain earnings while shareholders would prefer higher dividends. Retaining earnings works in the favour of managers who, because an increase in earnings reflects size growth, will attract greater power and influence to dominate the board and thus grant themselves higher pay (Jensen, 1986; 1993).

Earnings retention will cause managers to rely less on external financing when new investment funds are required (McColgan, 2001). Dividends can be viewed as a means to foster discipline amongst managers by stripping them of some funds that could be used when lucrative investments are identified. Managers will be forced to approach the debt markets to raise sufficient funds, which in turn will subject them to the discipline of constant interest payments and capital repayment (Firer et al., 2008). Easterbrook (1984) suggests that borrowing money externally will provide a useful monitoring mechanism that restricts managers from pursuing their own interests over those of shareholders. Hence, dividend payments are viewed in a positive manner as they restrict management's ability to act in self-interest. However, the view that increasing dividends will reduce free cash flow available to managers and force them to seek external funds implies that shareholders must accept the risk of high debt levels and also tolerate the submission of greater amounts of individual tax rates on dividends (Al Malkawi et al., 2010).

3.5 GLOBAL FACTORS AFFECTING DIVIDEND PAYOUT DECISIONS

Factors affecting dividend decisions vary. Various research has shown that factors such as leverage, firm size, growth opportunities and profitability have a strong correlation with dividend payout decisions (see **Figure 3.1** below). Previous research focused on the relationship between dividend payout decisions and financial factors such as profitability, leverage and investment opportunities while neglecting the relationship between dividend payout and other qualitative factors such as corporate governance quality, audit quality and ownership structures (Baker, 2008). Although the literature on these relationships is limited, recent studies examining these relationships have increased in number.

Figure 3.1 below provides a summary of recent empirical findings on the firm based and market based factors affecting dividend decisions. It also reflects the dividend conundrum where the determinants of dividend decisions are inconclusive and variable across countries and sectors.

Empirical study	Country	Dividend payout factors
Andrikoupolos, El-Ansary and Hassan (2020)	MENA region	Investor sentiment (-)
Taekyu and Injjong (2020)	Korea	Corporate credit rating (+)
Chee, Ab, Razak and Wong (2020)	Tiger Cub Economies	CEO Overconfidence (-)
Lotto (2020)	Tanzania	Profitability (+), Liquidity (+), Firm size (+), Leverage, (-) Firm growth, (-) Previous dividends, (+), GDP (-)
Bashir and Usman (2018)	Pakistan	Growth(-), Profitability(+), Previous dividend(+), Loan deposit ratio(-)
Morakinyo, David, Adeleke and Omojola (2018)	Nigeria	Firm size (-), Profitability(-), Board Independence (-), Board size (+), Financial crisis(-)
Al- Najjar and Kilincarslan (2018)	Turkey	Ownerships (-), Family involvement (-), Domestic financial institutions (-) Minority shareholder (-)
Anggorro and Yulianto (2019)	Indonesia	Institutional ownership (-), Public ownership (-), capital structure (+)
Dewasiri, Banda, Koralalage and Azeez(2019)	Sri Lanka	Previous dividend, Investment opportunities (-), Profitability (-), Firm size (-)
Forti et al. (2015)	Brazil	Company size (+), returns (+), market-to-book value (+), liquidity (+), control (+), profit growth (+), leverage (-), corporate governance (-), risk (-) and information asymmetry (-)
Ahmed and Murtaza (2015)	Pakistan	• Energy sector – earnings per share (+) and leverage (+) • Cement sector – liquidity (+) • Oil sector – earnings per share (+) • Sugar sector – earnings per share (-), firm size (+) and profitability (+)
Baa, Tawiah and Opoku (2014)	Ghana	Return on equity (+), profit after tax (+) and company size (+)
Arko, Abor, Adjasi and Amidu (2014)	Sub-Saharan Africa	• Other countries – profitability (+), investment opportunities (+), taxation (-), leverage (-), institutional shareholding (-) and risk (-) • South Africa – profitability (+), investment opportunities (+), company size (+), leverage (-) and risk (-)
Abor and Fiador (2013)	Sub-Saharan Africa	• Other countries – board composition (+/-), board size (-), chief executive officer duality (-), institutional shareholding (+) • South Africa – institutional shareholding (+)
Nnadi, Wogboroma and Kabel (2013)	Twenty nine stock exchanges in Africa	Profitability (+), company age (+), market capitalisation (+) and financial leverage (-)

Figure 3.1: Global studies on factors that influence dividend payout

Source: Adapted from Nyere and Wesson (2019).

3.6 FACTORS AFFECTING SOUTH AFRICAN DIVIDEND DECISIONS

South African studies have employed both empirical and survey methodologies to test various dividend theories and obtain dividend payout data from corporate managers, informing on how dividend decisions are made (Baker & Weigand, 2015). Prior to 2008, extensive studies were carried out to uncover the factors that led to certain dividend decisions in South Africa (Firer, Gilbert & Maytham, 2008). However, following the introduction of share repurchases as an alternative to cash dividends and dividend withholding tax between 2009 and 2012, limited literature exists to explain dividend behaviour in South Africa (Nyere & Wesson, 2019).

Firer, Gilbert and Maytham (2008) surveyed JSE listed corporate managers to uncover what factors they considered in making dividend decisions. They found that corporate executives saw the stability of earnings, investment opportunities, liquidity and maintaining smooth dividends as important considerations when deciding on dividend payout. Some 64 % of managers were reluctant to reduce dividends and emphasised on the importance of dividend smoothing to avoid the adverse effects associated with reducing dividends. Sibanda (2016) conducted a similar study and had results similar to Firer et al. (2008). The results also reflected on the reluctance of managers to reduce dividends, in line with the signalling theory of dividends.

Arko, Abor, Adjasi and Amidu (2014) studied the determinants of dividend decisions in sub-Saharan countries across various sectors. Their results revealed that South African managers consider the previous year's dividend and improvements in profitability when deciding on dividends. Firm size and higher growth opportunities were also found to be key determining factors in the dividend decisions of South African companies. Arko et al. (2014) concluded that dividend omissions and reductions embodied negative company fundamentals, namely increased earnings volatility risk and financial risk. They attributed these findings to the level of advanced analyst activity on the Johannesburg Stock Exchange, where company performance is under constant scrutiny. Hence, South African companies are hesitant to alter any dividend decisions, unless there are changes in fundamental performance, to avoid the negative consequences of dividend changes in an information efficient market. These results are consistent with the signalling theory of dividends (Arko et al., 2014).

Vermeulen and Smit (2011) examined the relationship between dividend payout and future earnings growth for JSE Listed firms across various industries between 1973 and 2009. They also compared this relationship against companies operating in the USA as a developed nation. Their results showed a significant positive relationship between dividend payout and

future earnings for South African companies. However, the results indicated a negative relationship between dividend payout and future earnings growth.

These results are contrary to Mtshali (2016) who observed an insignificant relationship between dividend payout and future earnings but a strong positive relationship with current earnings. The results showed that dividend paying firms were less likely to experience reduced earnings. This is in line with the signalling theory of dividends. After comparing their results to the USA and other developing nations, Vermeulen and Smit (2011) submit that factors affecting dividend decisions in South Africa are unique and cannot be treated as the same with other developing nations and developed countries.

Sibanda (2016) studied dividend payout policies and the appropriateness of Lintner's (1956) dividend smoothing model for firms listed on the JSE between 1995 and 2011. The results provided evidence supporting the dividend smoothing model for JSE listed companies. The results were consistent with findings by Firer, Muller and Viviers (2013) but in contrast with Wolmarans (2003) who concluded that Lintner's (1956) dividend model does not explain South African dividend payouts.

Abor and Fiador (2013) examined the effect of corporate governance and dividend payout policy in sub-Saharan countries. Their results reflected that good corporate governance in South African companies resulted in higher dividend payouts. Against the background of the agency cost theory, they posited that South African firms were willing to pay consistent dividends and seek external funding due to the ease of obtaining finance and the low cost associated with obtaining external funding. These results are consistent with Man-Kemp (2015) who also examined the relationship between corporate governance and dividend payout and found that as a proxy for corporate governance quality, South African companies with diversified boards tend to pay higher dividends.

Nyere and Wesson (2019) examined the factors that influenced dividend payout in South African listed firms. They concluded that the dividend policies of JSE listed companies are positively and significantly affected by company size and profitability. Furthermore, a significant negative relationship was observed between free cash flows and dividend payout. These results are in line with earlier studies that confirmed the reluctance of South African companies to change the size and pattern of their dividends even in periods of change in firm fundamental performance such as profitability and cash flows.

A comparison between available South African literature on dividend policy and global studies on the factors affecting dividend decisions suggests that there is a need for more relationships to be examined in dividend payout decisions in South Africa.

3.7 CORPORATE GOVERNANCE AND DIVIDENDS

The outcome and substitute hypothesis have been widely used to explain the relationship between corporate governance and dividend payout decisions (Elmagrhi et al., 2017). The outcome model suggests that in companies where shareholders carry strong rights to force managers into issuing dividends, agency costs are minimised. Hence, dividends are paid as a result of good quality corporate governance (La Porta et al., 2000). This is against the background of the agency theory, which suggests that dividends can be used as a monitoring device to discourage managers from using free cash flow to pursue their own interests (Jensen & Meckling, 1976). The outcome hypothesis postulates that lower dividends will be paid where investors have weak rights to force managers into paying dividends (La Porta et al., 2000).

The substitute hypothesis posits that dividends act as a substitute for shareholders' rights (La Porta et al., 2018; Atanassov & Mandell, 2018). In companies that exhibit good corporate governance and monitoring of managers, investors are not motivated to push for dividends because of the high trust that they have in the ability of managers to act in their interests (Atanassov & Mandell, 2018). However, where governance is weak, managers issue dividends to assure investors that they will act in the best interests of shareholders (Atanassov & Mandell, 2018). La Porta et al. (2000) suggest that managers in firms with poor governance are more likely to pay large dividends to maintain a reputation with investors.

Rahman and Khatun (2017) define corporate governance quality as “codes of governance, rules, regulations, and best practices related to governance and developed to assess whether firms are well governed or poorly governed firms.” This is in line with Waweru (2014) who submits that companies with good quality corporate governance are those that meet corporate governance standards set by regulatory authorities. Against this background, studies that have sought to investigate the relationship between corporate governance and dividends, firm performance and capital structure have used worldwide corporate governance codes, regulations and best practices to formulate measures for the quality of corporate governance.

A recent American study by Atanassov and Mandell (2018) examined the relationship between corporate governance and dividend payout. Its results agree with those of a study conducted by Elmagrhi et al. (2017) who used fiduciary waiver, mandatory distribution, voting rights and

ownership structure as their corporate governance variables. Their results revealed that firms with weaker governance were more likely to pay higher dividends, thus reducing firm value.

Elmagrhi et al. (2017) examined the relationship between corporate governance and dividend payout in UK listed small to medium enterprises (SMEs). The study employed board size, frequency of board meetings, board gender diversity and audit size as corporate governance variables. They found significant relationships between all the variables under study and dividend payout policy. Therefore, UK SMEs with weak governance mechanisms paid out higher dividends (Elmagrhi et al., 2017). This finding is supportive of the substitute hypothesis where dividends can act as a substitute for weak governance.

However, Shamsabadi et al. (2016) had different results when they examined the relationship between corporate governance and dividend policy in Australia between 2001 and 2013. The results of their study showed a significant and positive association between corporate governance and dividend payments. These results confirmed that Australian firms use dividends as a monitoring device and supported the outcome hypothesis of dividends. Their findings revealed that corporate governance plays an important role in reducing agency costs through the distribution of higher dividends.

A few South African studies have examined the relationship between corporate governance and dividend payout policy. The few known studies have used different variables and yielded conflicting results and hence, may require further study. **Table 3.2** below is a summary of the few available studies, based on an extensive review of literature, examining the relationship between corporate governance and dividend payout policy in South Africa. It summarises the variables used, the relationships found and ultimately the conclusions made on whether dividend payments are determined by strong or weak corporate governance structures. In other words, these are conclusions on whether dividend payments are an outcome of good corporate governance or a substitute for weak corporate governance.

Paper	Corporate governance variables used	Relationship with dividend payout decisions	Outcome/Substitute based
Papo (2016)	Board size Board composition CEO duality Institutional ownership	Negative Negative Positive Negative	Substitute

Mans-Kemp (2015)	Board composition	Positive	Outcome
	Board committees	Positive	
	Individual directors	Negative	
	Directors remuneration	Positive	
	Shareholding	Negative	
	Accounting and auditing	Positive	
	Risk disclosure and reporting	Positive	
	Corporate culture and behaviour	Positive	
	Sustainability reporting	Positive	
Abor and Fiador (2013)	Board size	Negative	Outcome
	Board composition	Positive/Negative	
	CEO duality	Positive	
	Institutional ownership	Positive	

Table 3.1: South African studies on corporate governance and dividend payout

Source: Author's own construction

3.8 RESEARCH GAPS

The review above has revealed the following research gaps:

- Most global studies investigate the impact of general firm characteristics such as profitability, financial leverage and cash flow (Mans-Kemp, 2015; Elmagrhi et al., 2017). Limited literature exists on the relationship between corporate governance characteristics and dividend payout policy (Elmagrhi et al., 2017). See **Figure 3.1** above.
- While the existence of a relationship between corporate governance and dividends payout has been proven empirically, it remains unclear whether dividend payout policy is a substitute, a complement or an outcome of good corporate governance especially in the South African context where prior research has had conflicting results (Abor and Fiador, 2013; Mans-Kemp, 2015 and Papo, 2016). Abor and Fiador (2013) and Papo (2016) used the same variables in their studies but arrived at different conclusions (see **Table 3.1** above).
- As discussed in the literature, board diversity is highly recommended by many corporate governance codes, including the King IV Code of Corporate governance. As far as the researcher could establish from the few existing studies on corporate governance and dividend payout policy, no South African study has focused on the relationship between board diversity characteristics and dividend payout. This relationship has been tested on firm performance in South African companies (Bryant, 2019). This study seeks to be the first to explore the effect of select board diversity variables on dividend payout decisions.

3.9 BOARD CHARACTERISTICS AND DIVIDEND PAYOUT

3.9.1 Gender diversity and dividend payout

According to Eluyela, Dahunsi, Tolase, Okere, Ogabi and Kafidipe (2019), there has been a growing global interest in examining issues of gender diversity amongst corporate governance scholars. Due to the growth in corporate governance studies, researchers have been motivated to investigate the impact of board gender diversity on various topics such as board supervision and monitoring (Adams & Ferreira, 2009; Lee-Hwei Khaw & Liam, 2018), firm performance (Marinova, Plantega & Remery, 2016; Dolamo, 2017; Bryant, 2019) and reporting quality and earnings management (Al-Shaer & Zaman, 2016). However, limited literature exists to investigate the impact of board gender diversity against the dividend outcome (Elmargrhi et al., 2017).

According to Okere, Eluyela, Lawal, Oyebisi, Eseyin, Popoola and Awe (2019), women have displayed social, economic, political, intellectual and legal capacity to influence corporate decision-making. A lack of board gender diversity exposes companies to litigation risk, which ultimately threatens corporate success, external networking and competitive advantage (Okere et al., 2019). Hence, board gender diversity has been one of the most encouraged forms of diversity in the boardroom.

Historically, males have had greater opportunities to participate in corporate boardrooms compared to females (Dolamo, 2017). A recent study by Deloitte (2017) on women in the boardroom revealed that women held only 16.9 per cent of global corporate board seats, 5.3 per cent of board chair positions, 4.4 per cent of CEO positions while 12.7 per cent held CFO positions. While the figures are significantly lower than those held by men, the study reported a notable increase in the amount of female participation in the boardroom.

A study by Grant Thornton (2014) revealed that approximately 25 per cent of top decision making roles were occupied by females, a far cry from those held by their male counterparts. Despite low numbers, South Africa still ranks fourth globally, for the percentage of women chairing boards (Deloitte, 2017). Although there is no direct legislation on board gender diversity, the codes implicit within the Broad-Based Black Economic Empowerment (BBBEE) Act have been very influential in facilitating the participation of black women in decision-making (Viviers, Mans-Kemp and Fawcett, 2017). The King IV Code of Corporate Governance not only recommends gender diverse boards but goes further to encourage all companies to set and publish race and gender targets for board membership (Institute of Directors, 2016) as a means to foster objective and effective decision-making.

Previously, the government of South Africa attempted to legally enforce gender quotas on company boards (Viviers, Mans-Kemp & Fawcett, 2017). In November 2013, the National Women Empowerment and Gender Equity Bill was brought before parliament. The bill sought to force companies to appoint an equal number of females as compared to males to sit on the board. This bill was not well received as critics argued that government should deal with other underlying issues of gender inequality such as education, before imposing gender quotas on boards (Viviers et al., 2017). Therefore, the debate on gender and diversity quota legislation in South Africa is still ongoing.

Mandatory gender quotas have been successfully implemented in other countries such as Spain, France and Belgium, who followed Norway's implementation of a 40% gender diversity quota (Viviers et al., 2017). Some have responded to the call for gender diversity by setting voluntary board gender quotas. An initial target of 25% gender diversity for all FTSE 100 companies was met with great enthusiasm. The benchmark increased to 33% before 2020 and efforts to reach this target are still ongoing (Thomas, 2020).

Women and ethnic minorities enhance decision making in organisations by bringing their unique contribution and perspectives to the board (Westphal & Milton, 2000). Konrad and Erkut (2006) postulate that company boards with three or more women make improved decisions by considering the perspective of multiple stakeholder groups. In addition, women are less likely to ignore difficult issues and rather deal with matters arising decisively (Kramer, Konrad, Erkut and Hooper, 2006).

There is growing evidence that gender diverse boards are more effective (Cumming, Leung & Rui, 2015). Some studies suggest that females tend to display greater work ethic, morality and decision making ability. Adams and Ferreira (2009) suggest that females attended more board meetings and displayed more diligence than their male counterparts. Other studies have shown that female directors are more cautious when making decisions and are less likely to go to great lengths to display overconfidence (Eckel & Fullbruun, 2015).

Cumming et al. (2015) report that gender diverse boards experience less fraud and insider trading. Female directors tend to be more sensitive to ethical issues, choosing to be concerned with agency problems and the legitimacy of the firm. In addition, female directors are more likely to involve themselves with more monitoring activities by sitting on monitoring related boards such as the audit committee and nomination committee (Adams & Ferreira, 2009).

Collectively, the extant literature views gender diverse boards as more effective at decision making and monitoring, display more ethical behaviour and show interest in reducing agency

costs. Against the background of the agency theory perspective of dividends, gender diverse boards are more inclined to pay higher dividends (Ye, Deng, Liu, Szewczyk & Chen, 2019).

A large number of studies agree that gender diverse boards pay higher dividends. Ye et al. (2019) examined the impact of board gender diversity on dividend payouts in a sample involving 22 countries between the period 2000 and 2013. The results revealed that board gender diversity plays a significant role in reducing agency problems and increases the dividend payout ratio. Earlier on, Chen, Leung and Goergen (2017) examined the effect that companies with female directors had over dividend payout. Their study involved 1500 companies between the periods 1997 and 2011. Their results were consistent with those of Ye et al. (2019). They concluded that companies with female directors issued out higher dividends because of increased monitoring activity.

Al-Rahahleh (2017) investigated the impact of corporate governance quality and board gender diversity on the dividend payout of non-financial companies listed on the Amman Stock exchange between 2009 and 2015. Their results showed that companies with strong corporate governance and gender diverse boards had a greater propensity to issue dividend payments, which were also higher.

A recent study by Eluyela et al. (2019) did not concur with the hypothesis that gender diverse boards have any impact on the propensity to pay dividends or on the amounts paid. They examined the impact of a gender diverse board on the dividend payout in Nigerian firms. Their results showed that female directorship did not significantly influence dividend payout in Nigerian firms.

Based on previous global research combined with the absence of literature on board gender diversity and dividend policy in South Africa, the following hypothesis was posed;

H₁: There is a relationship between board gender diversity and dividend payout.

3.9.2 Ethnic diversity and dividend payout

Ethnic diversity refers to a mix of individuals from different racial and religious backgrounds (Deloitte, 2017). It is one of the core elements of a diverse board. Various corporate governance codes promote the inclusion of different races and cultures on to the board of directors (UK Corporate Governance Code, 2018; Institute of Directors, 2016). Companies with boards that do not reflect the ethnic demography of the region in which they operate may symbolise weak corporate governance and may result in missed opportunities (Daily & Dalton, 2003; Singh & Vinnicombe, 2004; Singh, Vinnicombe & Johnson, 2001). In South Africa, only

30 per cent of directors on the JSE are African, Black, Coloured or Indian. These figures are an alarming reflection of transformation and equity given that black people make up 76 per cent of the population (Carrim, 2018).

Different ethnic groups maintain their cultural and religious beliefs and therefore bring their unique perspectives in corporate decision-making (Al-Dhamari et al., Ismail & Al-Gamhr, 2016). Furthermore, other researchers have found evidence supporting that board ethnical diversity enhances firm performance and contributes to the maximisation of wealth for shareholders (Marimuthu, 2008; Churchill, 2019).

There is a close relationship between ethnic and gender diversity in South Africa due to the country's unique political history (Viviers, Mans-Kemp & Fawcett, 2017). The majority of South African corporate boards are still dominated by white males (Carrim, 2018). This situation is still prevalent because of the apartheid policies that were previously in place to marginalise women and black people. Policies such as the BBEEE promote inclusivity of previously disadvantaged ethnic groups in high-level corporate decision-making positions (Carrim, 2018).

Many studies that have used board diversity characteristics to explain dividend payout have not used ethnic diversity as an explanatory variable. However, South Africa's unique position renders ethnic diversity a matter of great importance. This study seeks to uncover the role that board ethnic diversity can play in mitigating agency costs.

Al-Dhamari et al. (2016) investigated the effect of board diversity using both gender and ethnicity as variables. Their results showed that boards with ethnic diversity in Malaysia have higher dividend payouts. However, they concluded that this is dependent on the level of cash flow generated by the firm. Furthermore, the positive and significant relationship was only noted where a firm's ownership structure is concentrated in the hands of institutional investors. These results are consistent with those from a study by Byoun, Chang and Kim (2016).

Byoun et al. (2016) examined the impact of board diversity on dividend payout as a major corporate decision. The study employed gender and ethnic diversity as variables to test the hypothesis that diverse boards issue out higher dividends. They established interesting results showing that gender and ethnic diverse boards issued higher dividends than firms without gender and ethnic diverse boards. In addition, their results reflected a decrease in the amount of dividends where gender and ethnic diverse boards switched to being non-diverse boards. Therefore, diverse boards can address the free cash flow agency problem through the monitoring effect of paying higher dividends (Byoun et al., 2016).

Limited literature exists on the relationship between ethnic diversity and corporate decisions such as dividend payout. No such investigation has been observed in a South African context. Therefore, the findings of this research potentially have meaningful contribution to the policies seeking to increase ethnic diversity in boardrooms.

There are two aspects to be considered. First, empirical evidence has shown that diverse boards tend to reduce agency problems by increasing monitoring and independence (Byoun et al., 2016; Al-Dhamari et al., 2016; Al-Rahahleh, 2017; Chen et al., 2017). Second, there is a possibility however that ethnic diversity in particular may result in conflict and miscommunication amongst board members, thus reducing monitoring effectiveness. Therefore, the following hypotheses were posed:

H₂: There is a relationship between board ethnic diversity and dividend payout.

H₃: There is no relationship between board ethnic diversity and dividend payout

3.9.3 Average age of the board and dividend payout

Age diversity is widely encouraged by the resource dependence theory as well as other global codes of corporate governance (Institute of Directors, 2016; Madhani, 2017). In recent years, many studies have focused on diversity from a gender perspective. The resulting limitation is that the broad effects of other diversity aspects on various organisational outcomes remain unknown. A review of existing literature highlighted that the relationship between average age of the board and dividend payout is not well documented (Benjamin & Tenai, 2018).

Studies examining the relationship between average age of the board and financial performance have offered two perspectives. First, a negative relationship between age and financial performance has been observed. This relationship has been explained by the deterioration of cognitive abilities faced by older board members, which in turn has an adverse effect on the financial performance of the firm (Waelchli & Zeller, 2013). There is evidence, however, that diversity in age contributes to diverse perspectives in decision-making. Against this background, it is thought that a positive relationship can be observed between average age of the board and financial performance because older directors provide younger directors with knowledge and skills that are obtainable only through experience (Benjamin & Tenai, 2018).

Tahir, Rahman and Masri (2020) examined the relationship between various board characteristics and dividend payout. They found a significant positive relationship between average age of board members and dividend payout. However, these results differ from those

of Benjamin and Tenai (2018) who provided evidence of a non-statistically significant relationship between age diversity of the board and dividend payout.

Based on the empirical evidence above, the following hypotheses were posed:

H_4: There is a relationship between average age of the board and dividend payout.

H_5: There is no relationship between average age of the board and dividend payout.

3.9.4 Financial Expertise and dividend payout

According to the SOX (Section 407), a financial expert 'is a person who has experience in accounting or finance or has supervisory expertise'. There has been an increasing global emphasis on financial expertise on the board of directors following international accounting scandals such as Enron, HealthSouth, Tyco and Steinhoff International (Sarwar, Xiao, Husnain & Naheed, 2018). The loss of investor confidence that followed accounting scandals resulted in policymakers and the business community hypothesising that financial expertise can assist the governing board in monitoring a manager's financial reporting process (Ji, 2017). Corporate governance codes and legislation have emphasised the importance of including financial experts on the board of directors (SOX, 2002; Institute of Directors, 2016).

There has been a growing amount of literature on the effect of financial expertise on outcomes such as decisions, financial performance and reporting quality (Ji, 2017; Kibiya, Che-Ahmad & Amran, 2016; Lee & Park, 2019). However, very few studies have attempted to link financial expertise and dividend payout decisions. The agency explanation can be used to link financial expertise on boards with corporate financial decisions. Financial experts are more likely to impact agency costs through their monitoring role (Ji, 2017).

According to Qiao, Chen and Hung (2018), most corporate governance studies focus their attention on the monitoring role of the board of directors and undermine the advisory aspect. Financial expertise contributes to a better understanding of financial numbers, which provides the board with more optimal advice on expert related policies such as dividend policy (Ji, 2017).

Ji (2017) studied the relationship between financial experts and dividend payout policy on 1 500 S & P firms. They found that board financial expertise is negatively related to dividend payout ratio. These results are consistent with the substitution hypothesis that suggests that an effective board with more financial experts will choose to lower dividends because of the

opportunity costs associated with dividends when positive NPV projects are foregone (La Porta et al., 2000).

Sarwar et al. (2018) also examined the relationship between financial expertise and dividend payout behaviour in Chinese and Pakistani firms between 2009 and 2014. Their study revealed contrasting results between the two markets. They found that Chinese firms with more financial experts on their boards do not use dividends as a control mechanism as depicted by the negative association between board financial expertise and dividend payout. These results are consistent with the substitution hypothesis and corroborate earlier findings (Ji, 2017).

On the other hand, Sarwar et al. (2018) found that Pakistani boards with greater financial expertise paid out a higher level of dividends. These results show that Pakistani firms use dividend payout as a control mechanism for mitigating agency problems, in line with the outcome hypothesis.

Qiao, Chen and Hung (2018) performed a similar study on S & P 500 firms for the period 2005 to 2012. The study focused primarily on the relationship between accounting expertise of directors and dividend payout. The results of the study showed that firms with more accounting expertise tend to pay lower dividends due to stronger accounting conservatism. Hence, there is a negative association between board accounting expertise and dividend payout levels.

Against the background of the discussion above, the following hypothesis was posed;

H₆: There is a relationship between board financial expertise and dividend payout.

Control variables

3.9.5 Board size and dividend payout

Both South African law and the King IV Report do not provide an explicit number as to the size of the board of directors a company must have (Jingura, 2018). Section 66 (2) of the Companies Act merely sets the minimum number of directors depending on the type of entity. The King IV Report provides recommendations on aspects to consider when choosing company board size (Institute of Directors South Africa, 2016).

The outcome hypothesis posits that larger boards are more effective in monitoring and controlling the behaviour of self-serving managers because larger boards have a greater pool of experienced and skilled directors who can offer wider perspectives during the decision making process (Elmagrhi et al., 2017). This is expected to lower agency costs by reducing

free cash flow available for exploitation by managers through higher dividends. On the other hand, the substitution hypothesis posits that large boards are associated with serious communication problems that lead to poor governance and board effectiveness and will pay larger dividends as a cover up for poor governance (Jingura, 2018).

Historically, smaller companies have been known to achieve better firm performance (Elmagrhi et al., 2017). According to Yeung (2018), a small board comprising between seven to ten directors is more ideal. As outlined in the substitution hypothesis, smaller boards exhibit stronger governance and will most likely utilise free cash flows for positive NPV projects and do not feel pressured into paying out larger dividends to impress investors. **Figure 3.2** below is an illustration of the effectiveness of small boards in relation to bigger boards in big US firms with regards to maximising returns.

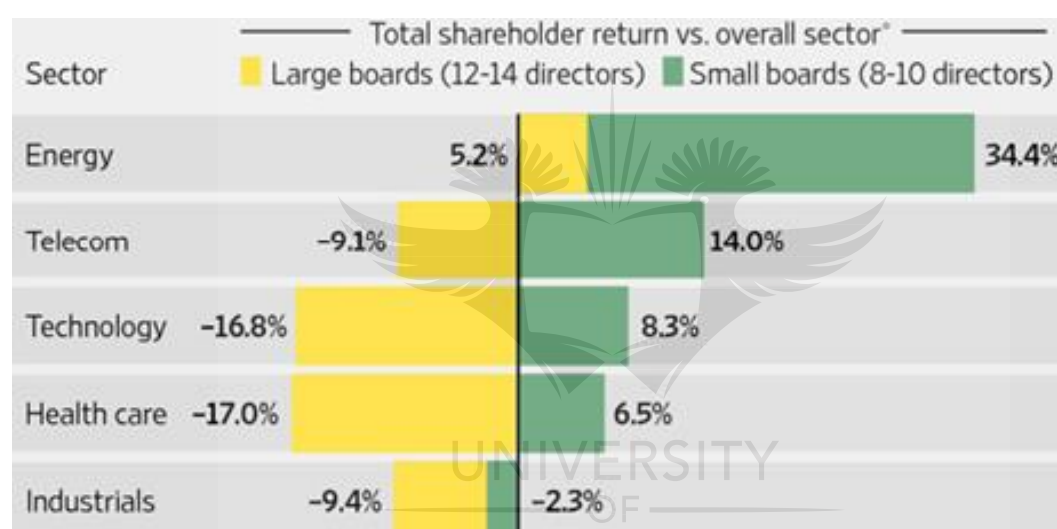


Fig 3.2: A comparison of shareholder returns generated by small boards vs big boards between 2011 and 2014 in large American firms

Source: GMI Ratings study of US companies with market capitalisation of at least \$10 billion (Wall Street Journal, 2014).

Nuhu (2014) examined the relationship between board size and dividend payout for Ghanaian firms between 2000 and 2009. The results from the study revealed a positive and statistically significant relationship between board size and dividend payout. This means that the greater the size of the board, the higher the level of dividends paid out due to increased monitoring activity. This result is consistent with studies by Mansourinia, Emamgholipour, Rekabdarkolei and Hoozori (2013) who also concluded there was a positive relationship between board size and dividend payout. In a later study, Elmagrhi et al. (2017) confirmed a positive relationship

between board and size and dividend payout amongst UK Small to Medium Enterprises between the years 2010 and 2013.

However, Ghasemi, Madrakian and Keivani (2013) found a negative and significant relationship when they examined the impact of board size and dividend payout. These results are consistent with those of the study by Papo (2016) and Abor and Fiador (2013) when they examined corporate governance and dividend payout decisions in South African firms. They found that as boards increased in size, dividends became lower.

Accordingly, the following hypothesis was posed;

H_7: There is a relationship between board size and dividend payout.

3.9.6 Board Independence and dividend payout

The King IV Report recommends that the board of directors should consist of a larger proportion of NEDs, most of whom should be independent (Institute of Directors South Africa, 2016). The resource dependence theory also encourages more outside directors due to the expertise, prestige and contacts they bring with them (Kesner & Johnson, 1990). The agency theory posits that increasing outside directors enhances monitoring and, ultimately, firm performance (Jensen & Meckling, 1976).

A number of studies testing the relationship between board independence and dividend payout have results that favour the substitution hypothesis (Abor & Fiador, 2013; Benjamin and Zain, 2015; Elmargrhi et al., 2017). Under the substitution hypothesis, a bigger number of outside than inside directors improves corporate governance practices and, accordingly, the board of directors has no need to issue out high dividends. Therefore a negative association is expected between a board with higher independent directors and the level of dividend payout.

Benjamin and Zain (2015) found that Malaysian firms with a greater proportion of outside directors paid lower dividends due to improved corporate governance practices. These results are consistent with similar studies elsewhere (Abor & Fiador, 2013; Papo, 2016; Elmargrhi et al., 2017).

Accordingly, the following hypothesis was posed;

H_8: There is a negative relationship between board independence and dividend payout.

3.9.7 Profitability and dividend payout

Profitability has been selected as one of the control variables in this study because of its ability to influence dividend payout decisions. Historically, profitability is considered as a primary indicator of a company's ability to pay dividends (Gill, Biger & Tibrewala, 2010). De Angelo et al. (2006) are of the view that profitable companies are more mature and less inclined to seek out multiple investment opportunities, which made them pay higher dividends.

Findings by Amidu and Abor (2006) and Anil and Kapoor (2008) revealed a positive relationship between profitability and dividend payout, confirming the hypothesis presented by De Angelo et al. (2006). In addition, previous studies have shown that profitable South African companies pay higher dividends than less profitable firms (Firer et al., 2008; Fusire, 2018; Nyere & Wesson, 2019).

However, Brook, Charlton and Hendershoft (1998) posit that dividend payout cannot be driven by one goal. Hence, the non-payment or low payment of dividends should not imply that a firm is not profitable (Ahmed, 2015). A profitable firm deciding that it has access to more lucrative investment opportunities, may choose to withhold dividends (Ahmed, 2015). The findings by Amidu and Abor (2006), Anil and Kapoor (2008) and Fusire (2018) of a positive relationship between profitability and dividend payout, provide a contrasting view to Lintner's (1956) belief that current profitability on its own was not sufficient to influence dividend payout. Instead, only a permanent change in earnings could affect dividend payout (Lintner, 1956).

Against this background, the following hypothesis was posed;

H₉: There is a positive relationship between profitability and dividend payout.

3.9.8 Previous dividend

Lintner's (1956) survey established that American firms aimed to maintain a pre-set targeted dividend payout ratio, which led to dividend smoothing over time. Lintner was of the view that only permanent changes in earnings would affect the current dividend payout.

Ozo, Arun, Kostov and Uzonwanne (2015) replicated Lintner's (1956) study to suit the Nigerian context. Their survey results revealed that for Nigerian companies, each year's dividend is dependent on the current earnings. Some managers alluded to considering the previous year's dividend when setting the year's dividend payout. However, 12 out of the 21 respondents highlighted that they only considered the previous year's dividend for comparison purposes.

Imran (2011) examined the determinants of dividend payout of Pakistan's engineering sector for thirty-six firms listed on Karachi Stock Exchange from 1996 to 2008. Results revealed a positive relationship between previous dividend and current dividend payout. These results are consistent with those of Dickens, Casey and Newman (2002) who submit that dividend history was an important factor in determining dividend payout.

Accordingly, the following hypothesis was posed;

H₁₀: There is a relationship between previous dividend and dividend payout.

3.10 CONCEPTUAL FRAMEWORK

The Conceptual Framework for the study is therefore summarised in **Figure 3.3** below.

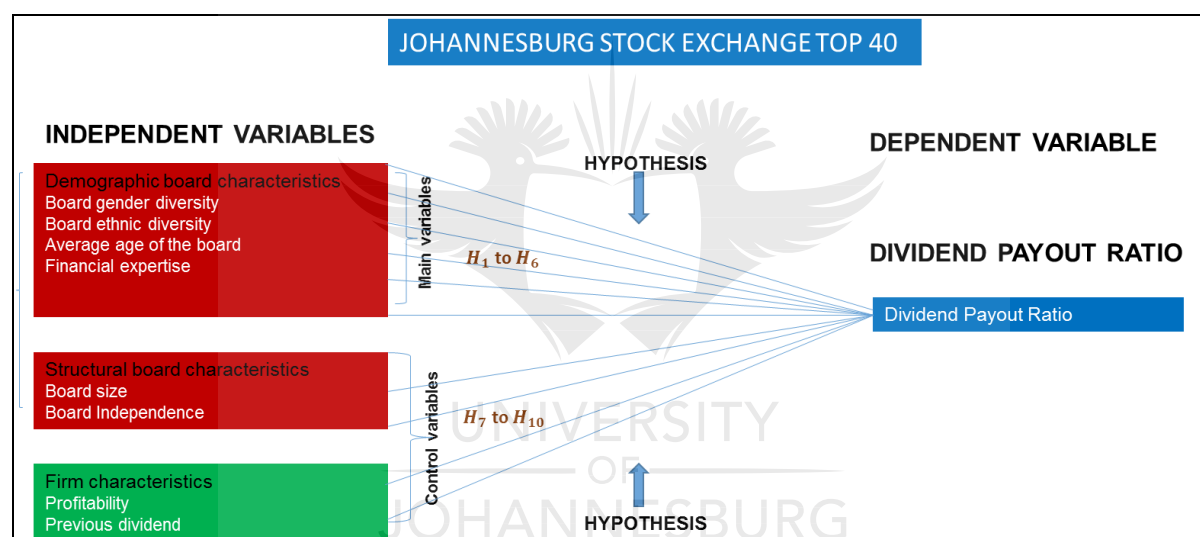


Figure 3.3: Conceptual Framework for the study

Source: Author's own conceptualisation

3.11 SUMMARY

The review revealed some research gaps in the extant literature. Existing literature on the factors that determine dividends has focused on the relationship that exists between accounting based variables and dividend payout. This relationship between corporate governance and dividend payout is under researched. This is surprising considering the increasing global interest in corporate governance related research. Existing studies have not

produced consistent results. Therefore, it remains unclear whether high dividends are an outcome or a substitute for good corporate governance practices.

Furthermore, it was established that the South African literature on board characteristics and dividend payout has investigated this relationship using board structural variables such as board size and board independence. This means that the effect of board demographic variables on dividend decisions remains unknown. The gaps uncovered in the literature have provided compelling motivation to continue with the study. The next chapter is a discussion of the research methodology adopted in to achieve the research objective.



Chapter 4 Methodology

4.1 INTRODUCTION

Chapter 3 of this study pointed out that it remains unclear whether the level of dividends paid is an outcome of the good governance quality or a substitute for the bad governance quality. It was indicated that the reason the evidence is inconclusive is that there are very few South African studies that have investigated this relationship. Furthermore, the few studies that have attempted to, have yielded mixed results.

Understanding this relationship within a South African context is important, given the recurrence of corporate scandals involving unethical practices (Jingura, 2018). The agency theory posits that one way to reduce agency costs is through the payment of dividends. Dividends achieve this by reducing the amount of free cash flows available for managers to use for their self-interests rather than for the benefit of company shareholders, thus inducing monitoring from external markets (Easterbrook, 1984). Furthermore, the resource dependence theory alludes to board diversity as having a great impact on firm decisions and organisational outcomes.

The main objective of this work was to examine the relationship between board characteristics and dividend payout using the top 40 companies listed on the JSE. This chapter describes the methodology that was followed to achieve the research objective. Essentially, this study can be described as a correlational study whose main emphasis was to ascertain the existence of a relationship, association or interdependence between two or more aspects of a situation or phenomenon (Kumar, 2019).

This chapter outlines procedures and methods used for data collection, sampling and data analysis. Section 4.2 discusses the research paradigms and Section 4.3 describes the panel regression method used to analyse the data. Details of the sampling strategy adopted for the study are discussed in Section 4.3. This is followed by a description of the methods used for data collection. Section 4.6 then discusses the research variables of the study. The ethical considerations are outlined in section 4.7 while validity and reliability are discussed in section 4.8. These are followed by a brief explanation of the limitations in section 4.9. The chapter ends with a summary in section 4.9.

4.2 RESEARCH PARADIGM

According to Creswell (2014), the plan to conduct research should be an extensive one, and it involves three elements, namely (1) the intersection of philosophy, (2) the research design and (3) the specific research methods. This is in line with earlier views by Easterby-Smith and Thorpe (1997) who posited that the exploration of philosophy is significant in the research methodology because it assists researchers in refining and specifying the overall research methods and strategy to be used. Furthermore, exploring research philosophy should influence the type of evidence gathered and analysed in order to answer the research question posed.

The research philosophy is a paradigm that is described by Granlund and Lukka (2017, p. 66) as a “systematic procedure that formerly guides the way a problem can be resolved”. According to Patel (2015), research paradigms are best expressed through ontology, epistemology and methodology. These terms are further explained thus;

- **Ontology** – refers to how the researcher views reality;
- **Epistemology** – is how the researcher can obtain knowledge by making a distinction between supported beliefs and opinion, and
- **Methodology** – refers to how the researcher obtains the required data, knowledge and understandings necessary for addressing the research problem.

According to Bless, Higgson-Smith and Sithole (2013), there are five paradigms in research. These are detailed below.

- The **positivist** paradigm – This paradigm is grounded in scientific research methods. It is built on the premise that understanding human behavior should be based on experimentation, observation and experience. According to Kivunja and Kuyini (2017), research conducted within this paradigm is reliant on the formulation and testing of hypothesis and statistical methods to derive conclusions. In addition, it is best suited for searching cause and effect relationships in nature. Patel (2015) explains that positivists are convinced that there can only be one reality, which can be measured by using quantitative research methods.
- **Interpretivism** - This paradigm is based on the premise that all knowledge is a matter of interpretation. Research conducted within this paradigm makes an effort to understand and interpret the views and thoughts of a subject. Hence, qualitative methods are best suited for this type of study (Kivunja & Kuyini, 2017).
- A **pragmatist** approach is “one that evaluates ideas or views in terms of their ability to be applied practically in resolving problems” (Jingura, 2018, p. 63). Pragmatists use the

method that is best suited to the research problem regardless of whether it is qualitative or quantitative. According to Creswell (2014), pragmatists recognise the weaknesses in qualitative and quantitative methods and hence perceive them as complementary. Accordingly, this paradigm follows the mixed-method approach, as described below.

- **Subjectivism** is a paradigm “whose ontology is the reality of what is perceived to be real and knowledge is purely a matter of perception” (Scotland, 2012, p. 11).
- The **critical paradigm** - This paradigm has its roots in social justice issues and is determined to address the socio-economic and political issues which lead to inequalities. This paradigm is also known as the transformative paradigm. It takes up a transactional epistemology, where the researcher interacts with participants through a dialogic methodology (Kivunja & Kuyini, 2017). Scotland (2012, p. 11) asserts that a critical paradigm “is where there is the reality that is constantly under the internal influence; thus, the reality and knowledge are both influenced by power and socially constructed”.

Given the nature of this work, a positivist research paradigm was deemed relevant.

- First, it was deemed relevant because it is best suited for studies seeking to ascertain the cause and effect of various relationships. In this regard, this study seeks to ascertain the relationship between board characteristics and dividend payout.
- Second, it was deemed relevant because the positivist paradigm is greatly reliant on the formulation and testing of hypotheses and statistical methods to derive conclusions. In this regard, this study has formulated several hypotheses, which is an element found to be consistent with the positivist paradigm.

4.2.1 Research method

The positivist paradigm is associated with the quantitative methodology. Hence, the quantitative methodology was adopted for the study. Sukamolson (2007) identifies four main quantitative research types, and these are described below:

- **The survey research** - According to Torchiano, Fernandez, Travassos and Mello (2017), survey research is a systematic tool used to analyse opinions, encounters and expectations. It is often used because of its ability to answer descriptive and explanatory questions useful for a researcher to understand what is happening and why it is happening. However, academics favour this method as an exploratory way to uncover an initial broad impression about a subject matter (Torchiano et al., 2017).
- **The correlational research**, commonly referred to as a regression analysis, is used to determine if and to what extent a relationship exists between two or more variables in an identified sample (Apuke, 2017). The main purpose of this type of research is to reveal the

direction and strength of a relationship between two or more identified variables (Senturk & Zeybek, 2019).

- **Experimental research** is a study that adopts a stringent scientific research design. It involves a hypothesis, a manipulable variable and variables that can be 'measured, calculated and compared' (Harland, n.d, p.1). This type of research is most suited for explanatory research, rather than for descriptive or exploratory research (Pelz, 2020). It can be referred to as hypothesis testing, in which the data and results obtained either support or reject the hypothesis.
- **Causal-comparative research** - According to Apuke (2017), the causal-comparative research is a study in which the researcher endeavours to uncover the cause for pre-existing differences in groups of individuals. Causal comparative research and correlational research are similar in that they both seek to establish relationships amongst variables. However, causal-comparative research is more reliable in providing evidence for the cause and effect of relationships.

Accordingly, this study deemed that correlation or regression analysis would be an important tool in the attainment of the objectives of this work, which sought to establish relationships between board characteristics and dividend payout.

4.2.2 Research instrument

A research instrument refers to the tools used to analyse the data. In line with previous studies of a similar nature, the panel regression was chosen as a suitable data analysis tool for the present study (**see Table 4.1**). The identified studies have used panel regression as a valid and reliable research instrument for ensuring objectivity. According to Simon (2011), validity and reliability are elements which must feature on any chosen research instrument because "the accuracy, transferability, dependability and credibility of information depend on these". This is in line with Mouton (2001) who suggested that validity is closely related to unbiased results obtained from an objective process, while reliability allows for any researcher using the same data to arrive at the same conclusion. Thomson (2011) posits that this repeatability will encourage the wider scientific community to accept the hypothesis.

Table 4.1 below shows studies that have agreed on the validity and reliability of the panel regression as a research instrument in carrying out investigations of a similar nature. In addition, these studies concur that panel data is the best way to capture variations over time.

Authors	Year	Title	Research Instrument
Tahir et al.	2020	Do Board Traits Influence Firms' Dividend Payout Policy?	Panel regression
Sarwar et al.	2018	Board financial expertise and dividend-paying behavior of firms	Panel regression
Elmaghri et al.	2017	Corporate governance and dividend payout policy in UK listed SMEs	Panel regression
Papo	2016	Dividend policy and corporate governance in emerging markets: The South African case	Panel regression
Shamsabadi et al	2016	Corporate governance and dividend strategy: Lessons from Australia	Panel regression
Mans-Kemp	2015	The relationship between corporate governance and dividend payout ratios: A South African study	Panel regression
Abor & Fiador	2013	Does corporate governance explain dividend policy in Sub- Saharan Africa	Panel regression

Table 4.1: Prior studies similar to the present study that have used the panel regression research instrument

Source: Author's own conceptualisation

4.3 PANEL REGRESSION ANALYSIS

A panel regression measures data that contains both time series and cross sectional elements (Brooks, 2013). This quality was considered useful for this research because the data for this study is characterised by both time series (annual firm variables from 2013 to 2018) and cross section dimensions (top 40 Companies listed on the Johannesburg Stock Exchange). All three types of panel data analysis are considered in this study. These are the pooled ordinary least squares method (pooled OLS), the fixed effects model and the random effects model (Brooks, 2013; Bless et al., 2013; Hidayat & Abduh, 2012).

An assumption is made, under the pooled regression model, that the mean is zero and that the variance is the same across all variables (Fusire, 2018). Hence, when all the data is combined, there is no distinction between the time series and cross section, which allows for an ordinary least squares regression (Hidayat & Abduh, 2012). One of the advantages of the pooled OLS is that it is simple and quick and compares well against sophisticated regression models. However, Permani (2009) cautions against the weakness of the pooled OLS where the observations are not balanced.

The fixed effects model aims to address the weaknesses of the pooled OLS regression. This is achieved by considering the heterogeneity or uniqueness of the variables under study. The fixed effects model assumes that the intercept coefficients are constant and are not varied across the independent variables (Brooks, 2013).

The random effects model is considered to be more attractive than the fixed effects model because “the observed characteristics that remain constant for each individual are retained in the regression model” (Hidayat & Abduh, 2012, p. 83). This is not the case in the fixed effects model, in which these constant observed characteristics have to be dropped.

To ascertain which one of these models is best suited for this study, several diagnostic tests were performed. To distinguish the better model between the pooled OLS and the fixed effects model, the redundant fixed effects test was applied. In contrast, the Hausman test was employed to compare the fixed effects model and the random-effects model.

To examine the relationship between board characteristics and dividend payout, the following econometric specification was applied to the study:

$$DPR_{it} = \gamma_1 + \gamma_2 BGEN_{2it} + \gamma_3 BETHN_{3it} + \gamma_4 CTEN_{4it} + \gamma_5 BFINEX_{5it} + \gamma_6 BSIZE_{6it} + \gamma_7 BIND_{7it} + \gamma_8 PROF_{8it} + \gamma_9 PREVDIV_{9it} + \epsilon_{it} \dots \text{ (Eqn 3.1)}$$

where:

DPR is a dependant variable representing the Dividend Payout Ratio;

BGEN is an independent variable representing Board Gender;

BETHN is an independent variable representing Board Ethnicity;

AVAGE is an independent variable representing Average Age of Board Members;

BFINEX is an independent variable representing Board Financial Expertise;

BSIZE is a control variable representing the Size of the Board;

BIND is a control variable representing the number of Independent Directors serving on a company's board;

PROF is a control variable representing a company's Profitability, and

PREVDIV is a control variable representing a company's Previous Dividend.

4.4 SAMPLING STRATEGY

There are two types of sampling methods, namely probability sampling and non-probability sampling (Setia, 2016). In probability sampling, each unit has a known zero chance of being part of a sample. In other words, each participant has a similar chance of being selected (Etikan, Musa & Alkassin, 2016).

Randomisation is not such an essential element in non-probability sampling as it is in probability sampling. In non-probability sampling, subjective methods are utilised to decide on participants, and hence, not all participants have equal chances of being involved (Etikan et al., 2016).

The study adopted a convenience sampling method, which is a type of non-probability sampling where participants are selected based on their ability to meet readily defined criteria such as the ease inaccessibility and the geographical proximity (Dörnyei, 2007). The convenience sampling method used in this study was purposive. This permitted the researcher to use personal judgment in selecting a sample best suited for attaining the research objectives.

4.4.1 Target population

The population parameter includes all the companies listed on the JSE. However, this study examines the relationship between board characteristics and dividend payout on the top 40 Companies listed on the JSE. Hence, the sample includes only the top 40 constituents of the JSE. The top 40 Index is designed to be an equitable reflection of the South African stock market performance (Courtney Capital, 2013). In addition, it constitutes 80% of the total market capitalisation and is accordingly deemed a key market indicator (Kotze, 2017). These factors provided a justification for the target population selection.

4.4.2 Sample selection

As discussed earlier, a purposive convenience sampling strategy was used on account of the ease of access to data. The sample was derived from defined criteria from which the following considerations were made:

- **Listing** – The company's primary listing must be on the JSE.
- **Dividend Payout Ratio and Board Characteristics** – The company should have paid out a dividend for at least a portion of all the six years under study (2013 to 2018). Any company with zero dividend payout in the whole period under study was eliminated from the sample (Mehta, 2012). However, if a company displayed inconsistencies in the payment of dividends it was maintained in the sample to capture the circumstances

surrounding these fluctuations (Fusire, 2018). Companies with a minimum of 7 out of the 8 independent variables for each year under study were included in the final sample.

- **Availability of audited integrated financial reports** – Only companies with audited integrated reports for the duration of the study were considered. This is because audited statements are perceived to be a reliable and comprehensive source of data (Štangová & Víghová, 2016). Moreover, the variables in this study relating to board characteristics were derived from a more detailed explanation of an entity's corporate governance structure that was found in an entity's integrated report. Generally, integrated reporting became mandatory for all JSE listed companies from March 2010, and therefore the ease in obtaining integrated reports is considered in the sample selection (Du Toit, Van Zyl & Schutte, 2017).
- **Period of study** – For the study to capture recent and emerging dynamics, only the six years from 2013 to 2018 were considered. Moreover, data from some earlier years was not readily available (Papo, 2016) and the quality of integrated reporting during earlier years was still at infancy stage (Du Toit et al., 2017), which would have posed challenges in obtaining corporate governance information for some of the companies.

Appendix 1 illustrates the top 40 Companies included in the final sample. It provides the list of companies identified in the original sample and provides a justification for the exclusion of some of the companies from the final sample.

4.5 DATA COLLECTION

The study focused on examining the relationship between various board characteristics and dividend payout in the top 40 companies listed on the JSE. In order to achieve the objectives of this study, two types of data were collected for the 2013 to 2018 period. To ensure that only companies with a primary listing on the JSE were included in the sample, the search criteria on the Equity RT database was limited to those companies with an active primary listing on the JSE. Based on market capitalisation, a list of the JSE top 40 companies was obtained from the Equity RT database.

Board characteristics of the identified companies were collected manually from their audited integrated annual reports. For credibility, these reports were sourced from official company websites.

In addition to board characteristics, this study made use of financial variables. These were obtained directly from the Equity RT database, a global data management company that specialises in financial market research. Once the data was obtained, it was stacked in an

Excel spreadsheet, in a format that allows for input into Eviews financial modelling software for the running of a panel data analysis.

4.5.1 Data analysis

Eviews is an econometric, statistical and forecasting software which is used to analyse data. Data analysis for this work was carried out using Eviews software version 11. This is in line with previous studies of a similar nature that used Eviews to run panel regression for empirical analysis (Khan & Meer, 2017; Oyedeko & Adeneye, 2017; Fusire, 2018; Jingura, 2018; Muda, Maulana, Siregar, & Indra, 2018). Once a panel regression was performed, the descriptive output results and regression output were analysed and discussed.

4.6 RESEARCH VARIABLES

In the literature review, hypotheses were developed based on past empirical evidence, regulations and corporate governance codes. These hypotheses involved explanatory variables that had to be clearly defined for the study. Contrary to previous South African studies, this study incorporated other variables that had not been studied in the past. These variables include board gender diversity, board ethnic diversity and board financial expertise.

Essentially, demographic board characteristics, which have often been neglected over structural characteristics, are the main independent variables for this study. An independent variable is a characteristic whose value affects that of another variable. However, it is not in itself affected by changes in the value of the other variable (Shukla, 2018).

Two structural board characteristics, size and independence, were also brought in as control variables. Control variables are widely used in correlational studies similar to this work (Idris, Ishak & Hassan, 2019; Gyapong & Afrifra, 2019; Shehu, 2015). They refer to variables that are not of primary interest to the study but are considered to be of importance due to the effect that they may have on the results. The role of a control variable is believed to be the reduction of potential omitted variable bias by incorporating other variables that might explain the changes in the dependent variable (Tshipa, 2017). The study could not include all, but only those that have been known to affect South African dividends.

Chapter 3 provided theoretical links and other explanations for the inclusion of these variables. For instance, the King IV suggests that the board should be structured in a way that promotes diversity across a variety of attributes such as knowledge, skills, experience, age, culture, race and gender to promote the effectiveness of the board. While some countries have introduced

specific diversity quotas, South African law is not specific as to the exact diversity numbers to be included in a company's board; rather, the King IV leaves it to the board to set its own diversity targets (Institute of Directors, 2016). Given this, the study deemed it important to include these variables.

It must be noted that the King Committee was reluctant to set out specific numbers, which could be the result of fearing that companies may begin to recruit out of formality, rather than for experience and expertise. For a similar reason, the King Committee was also hesitant to specify how long a CEO could stay in a position. It can be inferred that the King Committee feared that companies would lose competent and experienced CEOs because of time collapse, which would not be beneficial for the company's operations (Institute of Directors, 2016).

In Chapter 2, it was indicated that the board of directors holds the ultimate decision over the dividend payout in a company. It was therefore deemed important to examine the extent to which the chosen board characteristics affect the level of dividends paid out to investors.

4.6.1 Dependent variable

Dividend payout is the dependent variable in this study. It refers to the level of earnings or how much of earnings will be declared as a dividend (Fusire, 2018). In line with previous research, the dividend payout ratio measured by $\frac{\text{Dividend Per Share (DPS)}}{\text{Earnings Per Share (EPS)}}$ is used as a proxy for dividend payout (Adjaoud & Ben-Amar, 2010; Byrne & Connor, 2017; Khan & Ahmad, 2017).

4.6.2 Independent variables

4.6.2.1 Board gender diversity

Empirical evidence suggests that gender diverse boards are more effective at decision-making and display a greater interest at reducing agency costs. Hence, they are more likely to issue higher dividends (Cumming et al., 2015; Ye et al., 2019).

Researchers have used different measures of gender diversity. Some have used the percentage of female directors as a proportion of the size of the entire board (Adams & Ferreira, 2009; Liu et al., 2014; Gyapong et al., 2019), others have used indices (Campbell, Minguez-Vera, 2008; Mans-Kemp & Viviers, 2015; Al-Shaer & Zaman, 2016; Gordini & Rancati, 2017), while others have opted for dummy variables (Byoun et al., 2016; Ye et al., 2019).

A dummy variable is an independent variable which takes the form of either 0 or 1, based on predefined categories. This study makes use of a dummy variable for gender diversity and follows an approach which is supported in corporate finance related studies (Adusei & Appiah, 2016; Fabbri & Klapper, 2016).

One of the contributions of this study is to the ongoing debate on whether implementing board gender diversity quotas would improve organisational outcomes such as firm performance and monitoring activities. Hence, the study proposes a measure that would provide a clearer point of reference for policy makers specifically for the South African context.

Previously, the South African government proposed legislation that would see companies shift towards 50% female board representation, but this was not well received (Ferreira & De Villiers, 2011; Viviers et al., 2017). Countries like Norway have implemented a 40% board gender quota while FTSE 100 companies are progressing towards achieving a 33% target by the end of 2020 (Viviers et al., 2017; Thomas, 2020). Against this background, a recent South African study examining the effects of board diversity and firm performance deemed 33% an appropriate target to indicate board diversity representation (Mans-Kemp & Viviers, 2015).

Accordingly, the following categories and dummy variables were constructed;

Category of gender diversity	Value of dummy
Less than 33% of women on the board	0
More than 33% of women on the board	1

4.6.2.2 Board ethnic diversity

Ethnic diversity in boards may yield a positive or negative outcome in the decision making process. On the positive side, it allows directors of different cultures and backgrounds to bring meaningful diverse contributions to the board. However, cultural clashes and communication barriers could result in conflict and could hence have an effect on the financial decisions of a company, including that of dividend payout (Byoun et al., 2016; Al-Dhamari et al., 2016; Chen et al., 2017 & Al-Rahahleh, 2017). Similar to other studies of this nature, the researcher measures board ethnic diversity as all non-white (black) members of an entity's board expressed as a percentage of the entire board size (Taljaard et al., 2015, p. 444; Tshipa, 2017).

4.6.2.3 Financial expertise

SOX (2002) describes a financial expert as one who has experience in accounting and finance or a supervisory role, including financial duties. In line with other studies, this research measures financial expertise as the number of directors who hold accounting or finance qualifications and have experience working as an accountant, auditor, Chief Financial Officer (CFO), financial manager or in any other expert role in finance, expressed as a percentage of the entire board size (Custodio & Metzger, 2014; Ji, 2017; Sarwar et al., 2018).

4.6.2.4 Average age of the board

Some studies have shown that the average age of board members has an influence on corporate decision-making. Tahir, Rahman and Masri (2020) found evidence supporting a relationship between average age of board members and dividend payout. This study measures average age of board members as the total age of all board members divided by the total number of board members (Tahir et al., 2020).

4.6.3 Control variables

4.6.3.1 Board size

Under the outcome hypothesis, it is assumed that larger boards are more effective at controlling agency costs and as a result will issue higher dividends as a control mechanism (Yeung, 2018). Meanwhile, the substitution hypothesis suggests that smaller boards exhibit stronger governance than larger boards and, as a result will issue out lower dividends to take up lucrative projects (Nuhu, 2014; Elmaghri et al., 2017). In line with previous studies, board size is measured as the natural logarithm of total board size (Abor & Fiador, 2013; Gyapong et al., 2019).

4.6.3.2 Board Independence

King IV recommends thus; “The governing body should comprise a majority of non-executive members, most of whom should be independent”. Independent directors have more reason to signal their reputation and ability to the market. As a result, greater independence enhances internal monitoring through the payment of higher dividends (Sharma, 2011). Board independence is measured as the number of independent NEDs expressed as a percentage of the entire board size. This is line with previous studies (Sharma, 2011; Saeed & Sameer, 2017; Jingura, 2018)

4.6.3.3 Profitability

It is believed that profitable firms have more capacity to issue high dividends. This is based on a proposition by De Angelo et al. (2006) who view profitable firms as more mature and less likely to seek out multiple investment opportunities and hence are in a better position to distribute high dividend amounts. While Brook et al. (1998) maintained that the non-payment or low level payment of dividends was not a strong base to support that a firm was unprofitable, some researchers found evidence supporting the view of De Angelo et al. (2006) who emphasised that more profitable firms are more likely to pay high dividends (Firer et al., 2008; Nyere & Wesson, 2019). The study used return on assets (ROA) as a measure of profitability and obtained this variable directly from the IRESS database.

4.6.3.4 Previous dividend

It is possible that companies aim to maintain a pre-set targeted dividend payout ratio (Lintner, 1956). This view is supported by various researchers who found evidence linking historical dividend payments to current dividend payout (Dickens et al., 2002; Imran 2011; Fusire, 2018). In line with these studies, the lagged DPS ratio was used as a measure of previous dividend. This variable was obtained directly from the IRESS database.

4.7 ETHICAL CONSIDERATIONS

It is expected that all researchers, both students and staff members, apply for ethical clearance or exemptions for ethical clearance for all research conducted. In line with this requirement, the researcher applied for ethical clearance for research involving secondary data (no human participation).

The School of Accounting (SoA) at the University of Johannesburg, under which the present study falls, has a Research Ethics Committee whose main objective is to maintain the highest ethical standards of practice in research carried out under its jurisdiction. The SoA ethics committee meets monthly to adjudicate on all submitted applications. This is carried out under the mandate of the College of Business and Economics (CBE). Accordingly, ethical clearance was obtained from the university on 28 July 2020. **(See Appendix 2.)**

The use of secondary data meant that all data was obtained from publicly available financial statements, which reduced the need to obtain consent from the companies involved. Furthermore, this eliminated any threat to confidentiality.

4.8 VALIDITY AND RELIABILITY

Validity and reliability are essential aspects of any research project (Chivandire, Botha & Mouton, 2019). On one hand, the validity of a study has to do with ensuring that a concept is appropriately and accurately measured (Combs & Falletta, 2008). On the other hand, reliability is related to the extent to which the variables used can achieve the same results if applied to a similar situation on different occasions (Mouton, 2001). In this respect, the study ensured reliability by using publicly available data from company annual reports. This means that the study can be replicated using the same publicly available information. To ensure that the variables used are appropriate measures for answering the research questions, variables were identified from an extensive review of literature. This process allowed for the construction of hypotheses and clarification of possible linkages amongst variables.

Moreover, objective diagnostic tests (correlation analysis, Hausman and Redundant fixed effects) were carried out to determine the best model to interpret the results of the study. This was done to ensure both reliability and validity of the results obtained.

4.9 LIMITATIONS

The final sample size was small, as it only included 29 listed companies. In addition, the study was limited to the companies listed in the JSE top 40. This excluded smaller listed companies and non-listed SMEs. Furthermore, there are various measures of gender and ethnic diversity, but the measures used were limited to less advanced techniques.

4.10 SUMMARY

This chapter discussed the methodology used to conduct the research. This included the research paradigm, method, instrument, sampling strategy and the econometric specification of the study.

The sample included the top 40 Companies of the JSE for a six-year period between 2013 and 2018. Data for the purpose of independent variables was sourced from audited integrated reports of the selected companies. The top 40 listing was obtained from the Equity RT database. The financial data was sourced from the IRESS database. The dependent variable was the dividend payout, while board gender diversity, board ethnic diversity, CEO tenure, board financial expertise were independent variables. Variables such as board size, board independence, financial leverage and growth opportunities were control variables.

Consistent with previous studies of a similar nature, a panel regression analysis was applied in order to analyse data. All three types of panel analysis were applied, namely the pooled OLS, the fixed effects model and the random-effects model. This was done in order to take into account the advantages and disadvantages inherent in the use of each model. Chapter 5 contains the presentation and discussion of empirical results.



Chapter 5 Presentation of Results

5.1 INTRODUCTION

The previous chapter outlined the research methodology adopted to answer the research question: could relationships between additional characteristics of the board of directors and the dividend payout (DPR) in the top 40 JSE listed companies be established? This chapter presents the results from an empirical analysis of annual data for the top 40 JSE companies from 2013 to 2018.

Section 5.1 discusses the sample size. This is followed by a discussion in Section 5.2 of the descriptive statistics of the demographic and financial variables used in this study. Section 5.3 conducts a multicollinearity test to determine relationships between the independent variables and Section 5.4 provides a detailed explanation of the panel regression modelling process used to establish relationships between the dependant variable (dividend payout) and independent variables (gender, ethnicity, financial expertise, board independence, the board size, profitability and previous dividend). This is followed by acceptance or rejection of the research hypothesis in Section 5.5. To end the chapter, Section 5.6 is a discussion of the findings while Section 5.7 provides a summary of the chapter.

5.2 FINAL SAMPLE

This study analysed panel data of the JSE top 40 listed companies over six years (2013 to 2018). There were 29 companies in the JSE top 40 sample (73%) that remained in the final sample following the exclusion of companies that did not meet the selection criteria. analysed **(See Appendix 1 for a full list of the companies used in the sample.)** Some of the reasons for exclusion included:

- Companies that were new entrants in the JSE top 40 Index and therefore did not have complete sets of financial statements for the period under study.
- Companies that had more than one financial variable missing for each year under study were removed from the sample.

Except for these companies that did not meet the criteria for selection, all corporate governance data was available in the integrated reports of the identified sample. The financial variables, including ratios, were directly sourced from the IRESS database.

Table 5.1 below demonstrates how the final sample sector representation compared to the entire JSE. Missing data from the metals and mining industry significantly affected the distribution of sectors in the final sample.

JSE Sector	Entire JSE Sector Representation (%)	Final Sample Sector Representation (%)
Media	24.44	33.20
Metals and Mining	21.61	14.61
Mobile and Telecommunications	6.76	9.11
Financial Services	24.55	30.68
Consumer goods	11.85	11.37
Property	2.97	1.03

Table 5.1: Sector representation of the overall JSE and final sample of the present study using market capitalisation

Source: Author's deduction (Data: IRESS)

5.3 DESCRIPTIVE STATISTICS

This section analyses the descriptive statistics of the research data. Descriptive statistics are an important aspect of research, and are applied to summarise the data in a meaningful way (Holcomb, 2016). They provide key insights into the sample and the measures used in a research study (Mishra, Pandey, Singh, Gupta, Sahu & Keshri, 2019). Measures include average values, median values, standard deviations and measures of normality (Brooks, 2014). In addition, time series plots are used to establish patterns within the dataset during the observed period. The dataset was an unbalanced panel with a maximum of 174 observations (29 companies x 6 years).

5.3.1 Dividend Payout Ratio (DPR)

Table 5.2: Descriptive statistics of the DPR in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
DPR	174	0.423929	0.424659	3.115538	-7.435065	0.701515	-7.458200	94.10509

Source: Eviews output

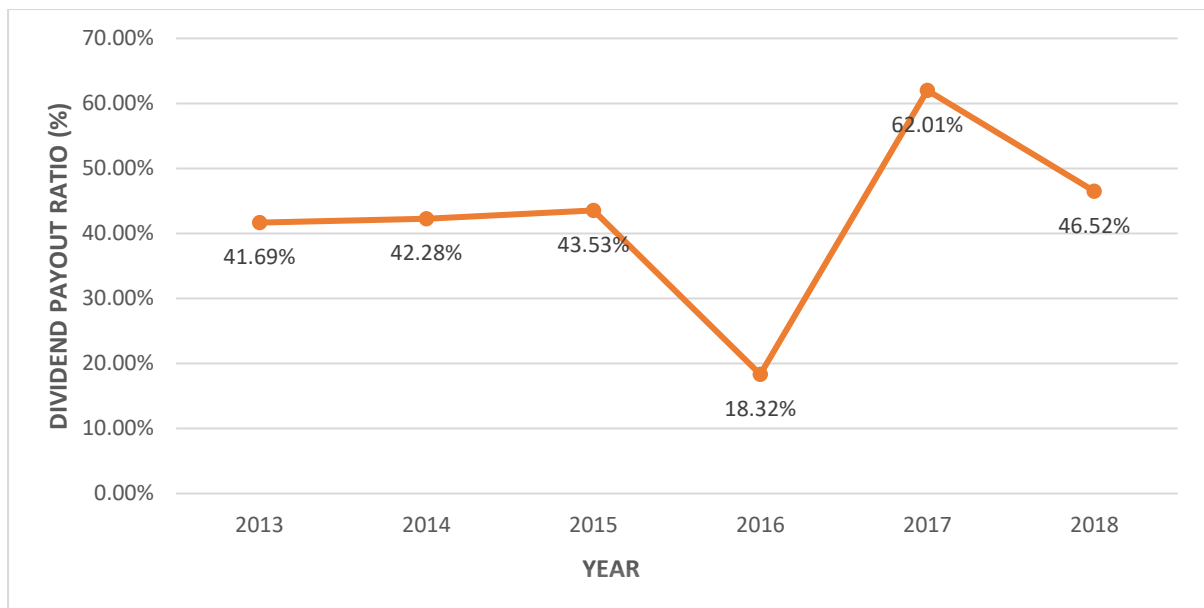


Figure 5.1: Average Dividend Payout Ratio of JSE top 40 companies

Source: Author's deduction (Data: IRESS)

The results presented in **Figure 5.1** above demonstrate that the JSE top 40 companies maintained a stable dividend over time despite the sharp decline in DPR experienced in 2016. A notable increase in DPR followed in 2017 before returning to 46.52%, a value closer to the average of 42.39% as outlined in Table 5.2 above.

The DPR ranged from 18.32 % to 62.01% over the six years under study. The kurtosis for the DPR was 94.11. Kurtosis is a measure of normality which measures whether data in a series is heavily or lightly tailed in comparison to a normal distribution. Data sets that have a high kurtosis, usually higher than 3, indicate that there are outliers in the data. As per the definition, a kurtosis of 94.10 indicates that there are outliers within the data (Brooks, 2014). The study deemed it necessary to maintain this data as meaningful insights could be obtained from it.

The lowest DPR was experienced in 2016, while the highest DPR was recorded in 2017. The sharp decline in 2016 can be explained by events taking place in the mining industry during the observed period. The 10-year trend analysis by PWC (2018) revealed that the dividend paid by the global mining industry in 2016 was the lowest since 2009. This is confirmed in the sample, where the only companies that did not declare a dividend in 2016 came from the mining industry.

Another possible reason the average DPR was lower in 2016 is that the DPR measure used in this study is calculated using Earnings per Share (EPS) and hence, creates a negative DPR

where a company records negative headline earnings. In 2016, the MTN Group suffered substantial losses in earnings due to a Nigerian regulatory fine that had a material impact on the company's financial position. This may have some contribution to the sharp decline in DPR in 2016 within our sample. A sharp increase in DPR followed in 2017 before returning to 46.52%, a value closer to the average of 42.39% as outlined in **Table 5.2** above.

5.3.2 Profitability

Table 5.3: Descriptive statistics of the ROA in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
ROA	174	9.18	6.08	63.73	- 17.12	12.66	1.23	4.85

Source: Eviews output

Figure 5.2 below shows the time series graph of profitability as measured by the ROA ratio from 2013 to 2018.

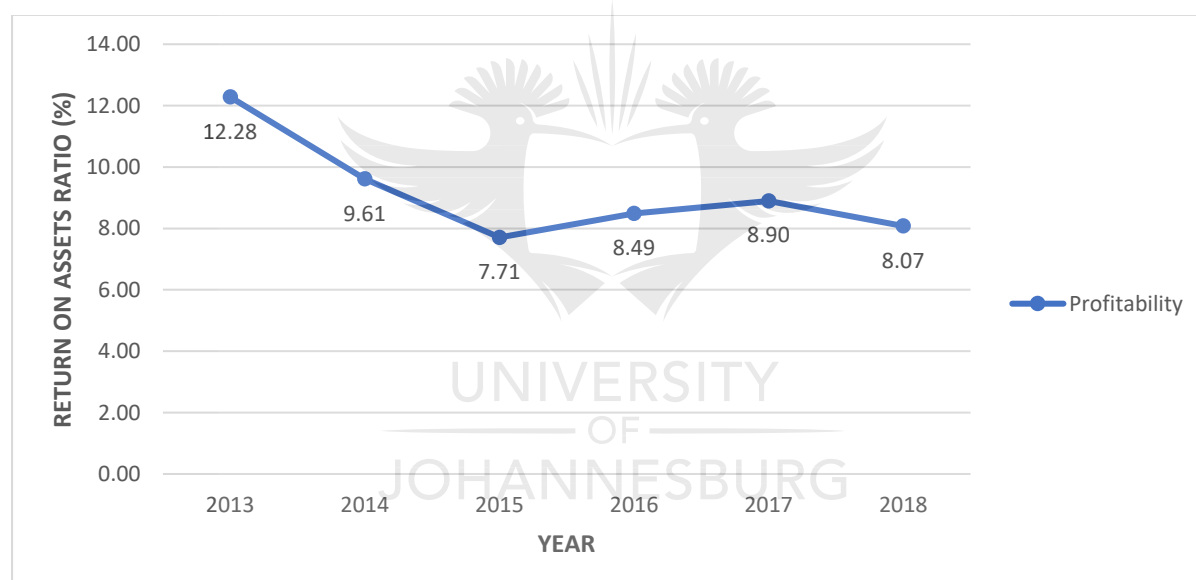


Figure 5.2: Average Return on Assets of JSE top 40 companies

Source: Author's deduction (Data: IRESS)

Figure 5.2 above shows that JSE top 40 companies maintained stable profits during the period under study. This is consistent with the profile of companies in the JSE top 40, which are inherently stable and mature (Intelligex, 2019). The yearly ROA values ranged between 8.07% and 12.28%. The skewness of 1.23 and kurtosis of 4.85 indicate that the majority of companies had ROA values more significant than the sample mean of 9.18%.

5.3.3 Gender diversity

Table 5.4: Descriptive statistics of gender diversity in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
Board Gender	173	0.204	0.20	0.50	0.0000	0.10	0.52	3.56

Source: Eviews output

Figure 5.3 below shows the time series graph of board gender diversity from 2013 to 2018.

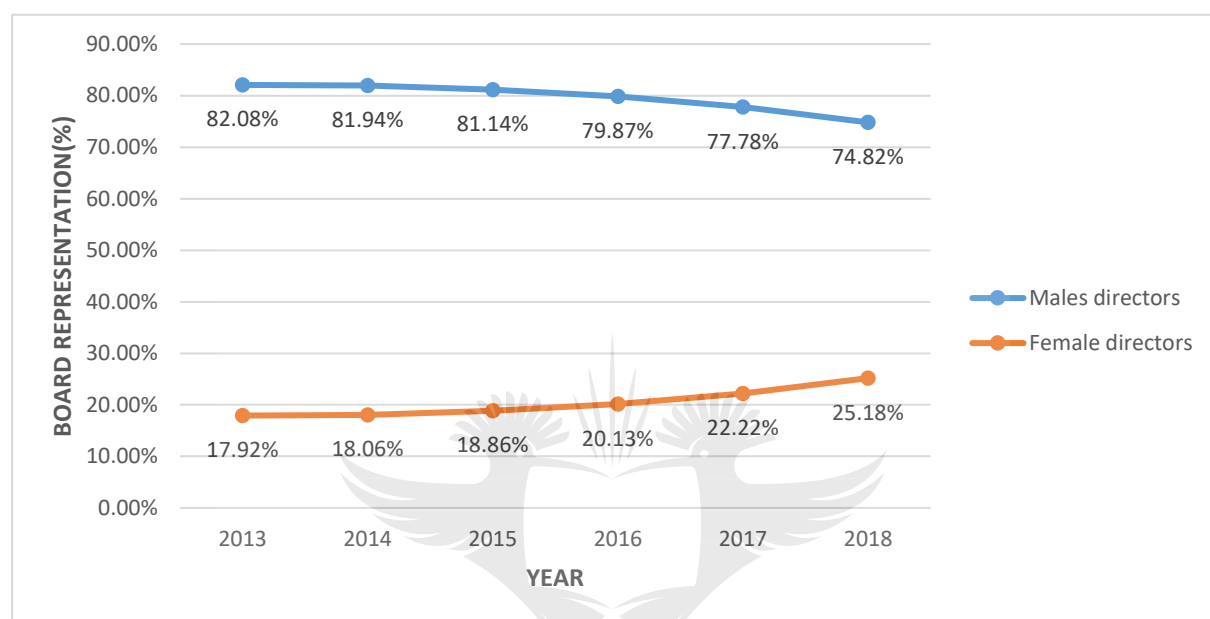


Figure 5.3: Gender board representation in JSE top 40 companies

Source: Author's deduction (Integrated Annual Reports)

The results presented in **Figure 5.3** and **Table 5.4 above** show that JSE top 40 boards remain dominated by male directors. Female representation of boards was as low as 0% in some companies, while the highest female board representation achieved was 50%. On average, over the duration of the study, there were only 20.4% females sitting on JSE top 40 corporate boards.

Figure 5.3 demonstrate that there was less than a percentage increase in female board representation between 2013 and 2015. A slightly greater percentage in females serving on JSE top 40 boards is observed between 2016 and 2018. This may be explained by the increased emphasis on gender diversity contained in the King IV Report that was published in 2016 (IoD, 2016). Although the results show steady progress, they also indicate that there are still factors hindering women from participating in corporate directorate positions. Data shows

that at the time when there was an increase in female representation, male directors were declining.

5.3.4 Ethnic diversity

Table 5.5: Descriptive statistics of ethnic diversity in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
Board Ethnicity	173	0.36	0.33	0.75	0.07	0.15	0.50	2.83

Source: Eviews output

Figure 5.4 below shows the time series graph of board ethnic diversity from 2013 to 2018.

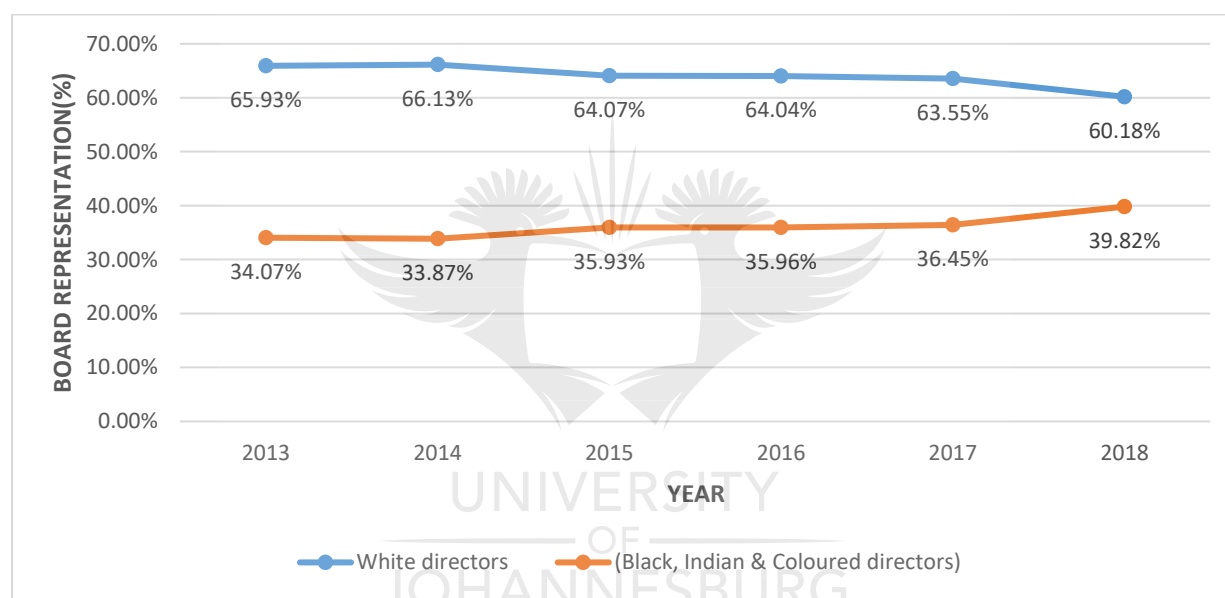


Figure 5.4: Ethnic board representation in JSE top 40 companies

Source: Author's deduction (Integrated Annual Reports)

The results in **Figure 5.4** and **Table 5.5** demonstrate that on average JSE top 40 boards comprise 36.22% black directors (Blacks, Coloureds and Indians). This figure does not reflect the demographics of the South African population. According to the StatsSA (2019) midyear report, black people constitute 92.1% of the South African population. The maximum representation of black people in some companies in some years was 75% and the minimum in some years was 7.14 %. Although the time series plot reflects steady increases in ethnic representation over the observed period, there is an indication that more transformation efforts should be expended to deal with inequalities when it comes to the representation existent in

corporate boards. This situation is not unique to the South African landscape. According to Cheng, Groyberg and Healy (2020), a similar picture is painted in America where 37 % of S & P 500 did not have black board members and only 4.1% of Russell 3000 board members in 2019 were black.

5.3.5 Average age of the board

Table 5.6: Descriptive statistics of average age of the board in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
Average age of the board	173	56.56	57.00	64.00	48.00	3.17	-0.30	2.92

Source: Eviews output

Figure 5.5 below shows the time series graph representing the average age of board members from 2013 to 2018.

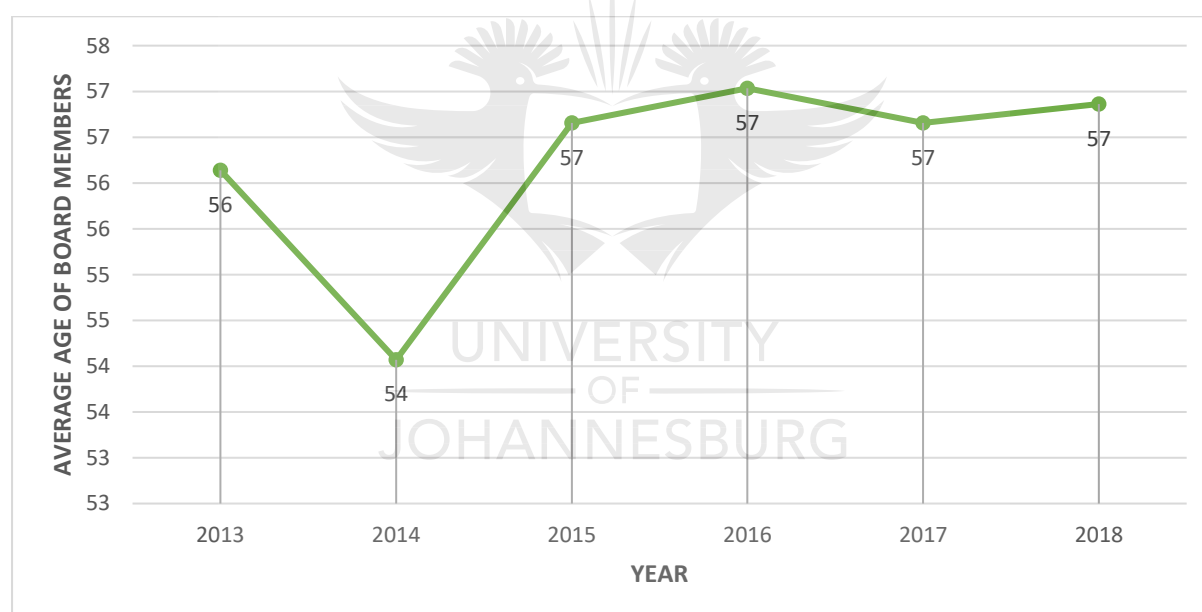


Figure 5.5: Average age of board members in JSE top 40 companies

Source: Author's deduction (Integrated Annual Reports)

The average age of JSE top 40 board of directors 56.6 years during the observed period. There was no large variation in the average age of the board with members averaging between 54 to 57 years of age over the six-year period. The youngest board member in the sample was aged 48, while the oldest board member was aged 64. The distribution is negatively skewed suggesting that a greater proportion of the directors in JSE top 40 boards are younger than the sample mean. In addition, the descriptive statistics suggest that predominantly

middle-aged directors govern JSE top 40 boards. This is under the presumption that individuals aged between 35 and 59 are classified as middle aged (Swart, Buthelezi & Seedat, 2019).

5.3.6 Financial expertise

Table 5.7: Descriptive statistics of financial expertise in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
Financial Expertise	173	0.4361	0.4375	0.8000	0.0833	0.1407	0.0260	2.6406

Source: Eviews output

Figure 5.6 below shows the time series graph representing the financial expertise of board members from 2013 to 2018.

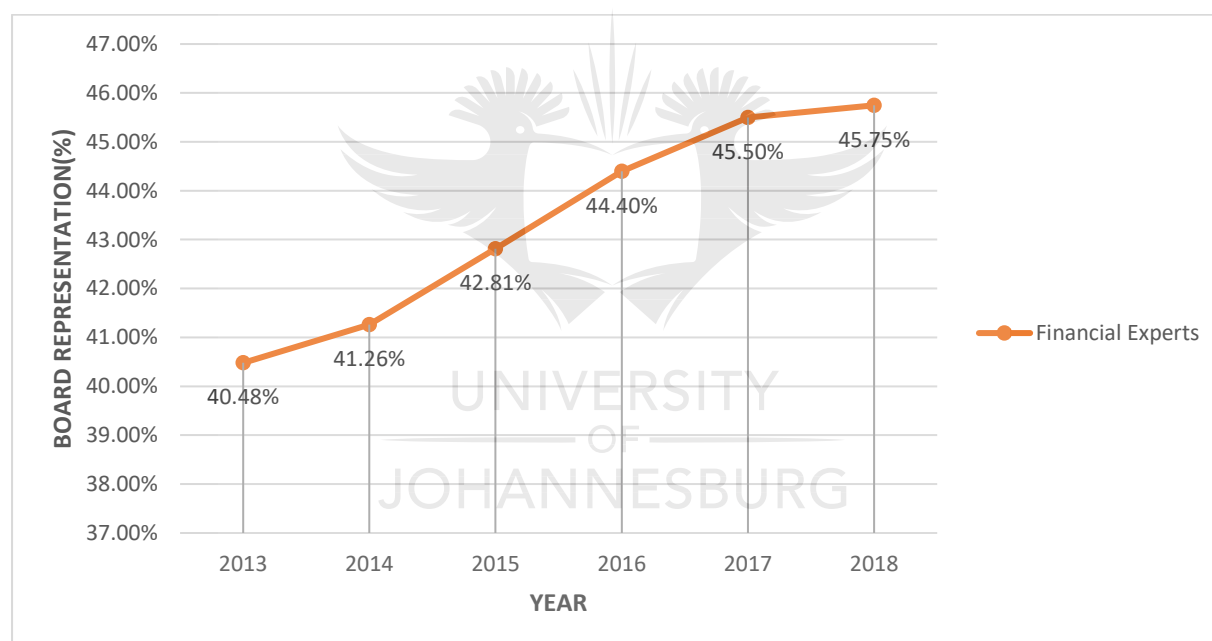


Figure 5.6: Financial expertise within JSE top 40 companies

Source: Author's deduction (Integrated Annual Reports)

The results above indicate that a significant proportion of directors in the sample are financial experts, with 43.61 % of directors in the JSE top 40 holding accounting and or a finance qualification and possess the necessary experience. Figure 5.6 suggests that the number of financial professionals on JSE top 40 boards rose steadily during the period of observation.

5.3.7 Board size

Table 5.8: Descriptive statistics of board sizes in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
Board size	173	14.27	14	21	9	2.903718	0.296163	2.411147

Source: Eviews output

Figure 5.7 below shows the time series graph representing the average board sizes in the JSE top 40 Companies from 2013 to 2018.

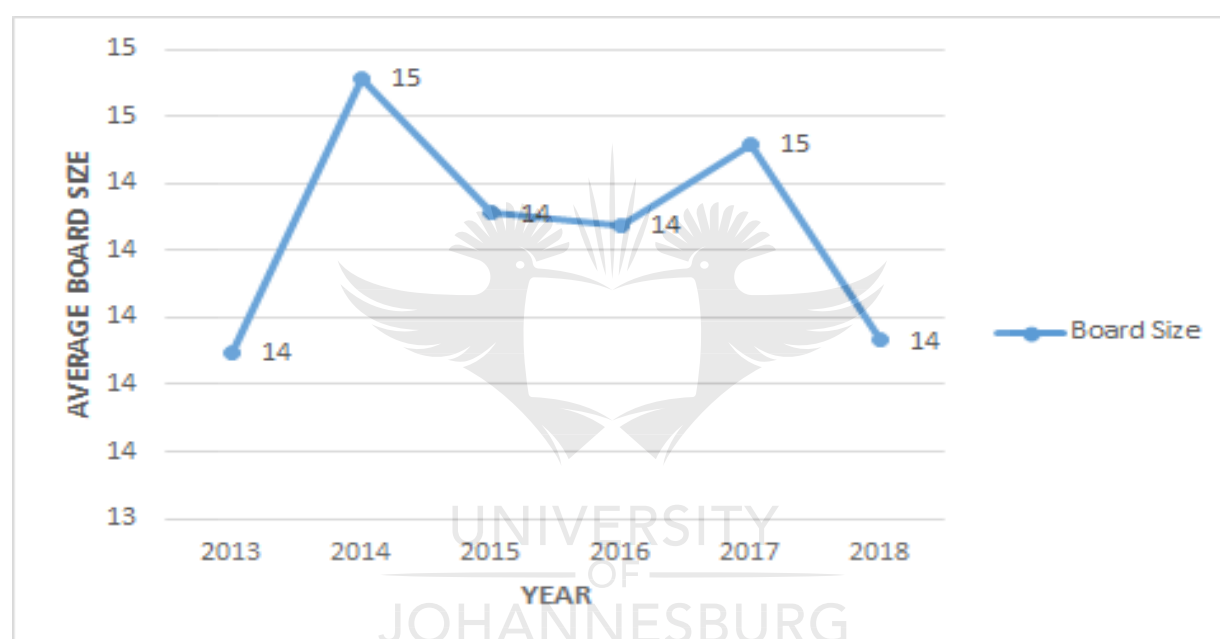


Figure 5.7: Average board sizes in the JSE top 40 companies

Source: Author's deduction (Integrated Annual Reports)

The results from **Table 5.8** indicate that, on average, JSE top 40 boards are made up of 14 members. This is consistent with the work by Taljaard et al. (2015) suggesting that this average has remained constant over the years. In their work, Taljaard et al. (2015) found that on average, 14 board members led the JSE top 40 boards between 2000 and 2013. The table above shows that the smallest board in the sample had nine members, while the most giant board had 21 members. Larger board sizes were observed in the Financial Services sector. This is in line with Walker (2009) who found that UK banks had larger board sizes than any other listed companies, and this was due to their complex organisational structure.

5.3.8 Board Independence

Table 5.9: Descriptive statistics of board independence in the JSE top 40 companies

Variable	Obs	Mean	Median	Max	Min	Std Dev	Skewness	Kurtosis
Board Independence	173	0.5495	0.5714	0.8461	0.2857	0.1302	-0.0561	2.1510

Source: Eviews output

Figure 5.8 below shows the time series graph representing the percentage of independent outside directors from 2013 to 2018.

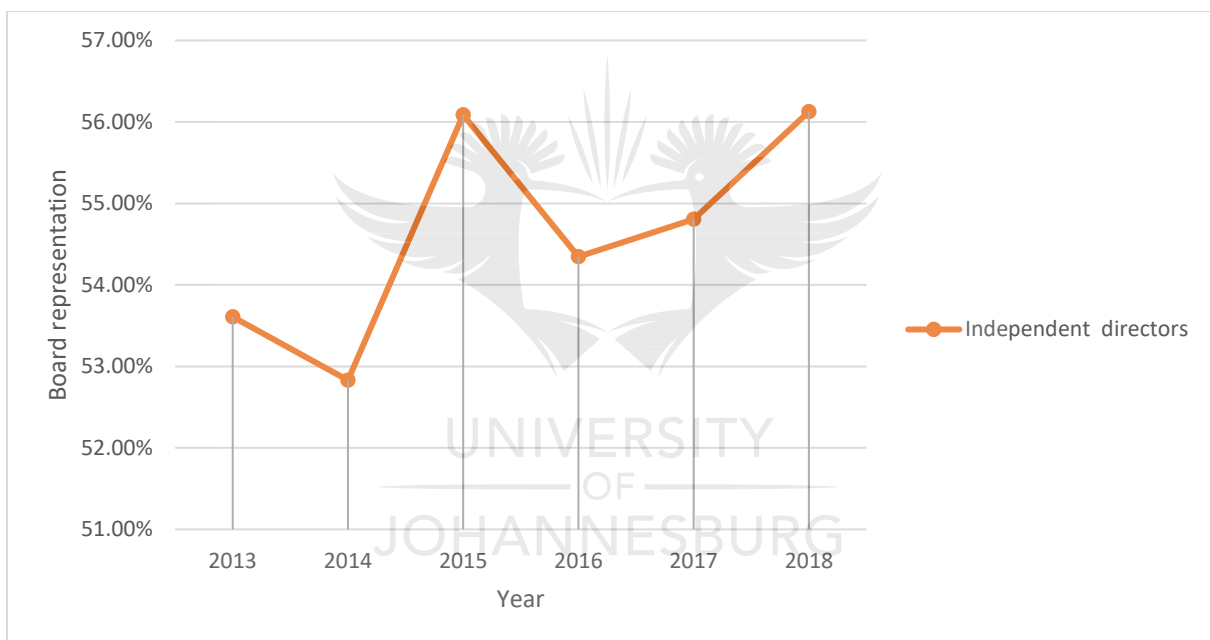


Figure 5.8: The percentage of Independent board members in the JSE top 40 Companies

Source: Author's deduction (Integrated Annual Reports)

Table 5.9 above reveals that the maximum representation of outside directors within the sample was 84.61%, while the lowest representation was 28.57%. On average, 54.95% of JSE top 40 board members within the sample were independent directors. **Fig 5.8** shows that during the period under observation, board independence among the JSE top 40 remained over 50%. The kurtosis of less than 3 indicates that there were very few outliers. The King IV

Report proposes that company boards should balance between skills, experience, diversity and independence of the directorate. Furthermore, it suggests that a lead independent director be appointed as chair of a governing body to enhance objectivity in the discharge of the board's core functions (Institute of Directors, 2016).

5.4 CORRELATION ANALYSIS

The presence of a high correlation between independent variables creates problems in interpreting regression results. When variables are highly correlated, their unique contribution to the prediction of the independent variable may not be visible. The extent to which multicollinearity poses a challenge to data interpretation depends on the degree of collinearity. There is a consensus amongst researchers that acceptable collinearity levels range between 0.7 and 0.9 (Gujarati, 1995; Kennedy, 1999; Fusire, 2018). This study applies a stricter limit of 0.7 as suggested by Tabachnick and Fidell (2001).

The collinearity between the independent variables is presented in the **Table 5.10** below.

	<u>DPR</u>	<u>PrevDiv</u>	<u>Bsize</u>	<u>Bgen</u>	<u>Bethn</u>	<u>Finex</u>	<u>Avage</u>	<u>Bind</u>	<u>ROA</u>
<u>DPR</u>	1.0000	0.2620	0.0048	0.0097	0.0616	0.0164	-0.0259	-0.1249	0.0930
<u>PrevDiv</u>	-0.2620	1.0000	-0.0435	0.0116	0.0643	0.0058	-0.0204	-0.0446	0.0926
<u>Bsize</u>	0.0049	-0.0434	1.0000	-0.3175	-0.0877	-0.1123	-0.0287	-0.1495	-0.3351
<u>Bgen</u>	0.0097	0.0116	-0.3175	1.0000	0.2515	0.0408	-0.0293	0.1460	0.2682
<u>Bethn</u>	0.0616	0.0644	-0.0877	0.2515	1.000	-0.0554	0.0773	0.3291	0.0699
<u>Finex</u>	0.0164	0.0058	-0.1123	0.0408	-0.0554	1.0000	-0.3228	-0.2473	0.0903
<u>Avage</u>	-0.0259	-0.0204	-0.0287	-0.0293	0.0774	-0.3228	1.0000	0.3342	-0.2203
<u>Bind</u>	-0.1249	-0.0446	-0.1495	0.1460	0.3291	-0.2473	0.3342	1.0000	0.0092
<u>ROA</u>	0.0930	0.0926	-0.3351	0.2682	0.0699	0.0903	-0.2200	0.0092	1.000

Table 5.10: Correlation analysis

Source: Eviews output

The highest correlation, at almost 34%, exists between board size and profitability, as measured by ROA. Slow decision-making and communication challenges associated with larger boards can be an obstacle to change and, as a result, it negatively affects firm performance, hence the negative correlation (Bennedsen, Kongsted & Nielsen, 2008). The results demonstrated in the table above also display a moderate positive correlation between gender representation and profitability as measured by ROA. This is expected since literature on gender diversity suggests that women bring their unique perspectives to the board and

hence, boards with more extensive female representation achieve higher firm performance (Westphal & Milton, 2000). Overall, the correlations demonstrated in **Table 5.10** are considered acceptable as none of them surpass a 0.7 benchmark.

5.5 PANEL REGRESSION

Panel regression analysis was used to examine the relationship between board gender, board ethnicity, and financial expertise, average age of the board, board independence, board size, previous dividend, profitability, and the dividend payout ratio. Three separate models were considered for the regression, namely the pooled Ordinary Least Square (OLS) regression, the fixed effects regression and the random effects regression. The fixed effects model was applied to address the weaknesses of the pooled OLS model, which does not consider the individuality of the companies in the sample. It assumes that the intercept is the same across all companies. Similar to the fixed effects model, the random-effects model accounts for heterogeneity but slightly differs in its assumption that heterogeneity is not correlated with the independent variables.

Diagnostic tests were performed to determine the best model for interpretation. The Hausman test was applied to decide between the random effects model and the fixed effects model. Furthermore, the redundant fixed effects test was conducted to determine the preferred model between the fixed effects model and the pooled OLS.

5.5.1 Empirical Analyses of Results

	Pooled Regression		Fixed Effects Regression		Random Effects Regression	
Variable	Coefficient	P-value	Coefficient	P-value	Coefficient	P-value
C	0.1008	0.9433	-2.2646	0.3604	0.1008	0.9427
Bgen	-0.0443	0.7974	0.1444	0.6490	-0.0443	0.7953
Bethn	0.6704	0.0844*	2.3440	0.0279**	0.6704	0.0813*
Finex	-0.0857	0.8293	0.8871	0.2603	-0.0857	0.8275
Avage	0.0107	0.5626	0.0055	0.8383	0.0107	0.5585
Bind	-1.0770	0.0193**	-2.1153	0.0201**	-1.0770	0.0181**
Bsize	0.0620	0.8277	0.8560	0.1417	0.0620	0.8529
PrevDiv	-0.2912	0.0001***	-0.3939	0.0000***	-0.2912	0.0001***
Prof	0.0075	0.0994*	0.0209	0.0391**	0.0075	0.0959*
R-squared	0.12		0.29		0.12	
Adjusted R-squared	0.08		0.10		0.08	

F-Stat	0.006***		0.0481**		0.006***	
*, **, ***, indicate statistically significant coefficients at 90%, 95% and 99% confidence levels respectively						

Table 5.11: Regression results

Source: Eviews output

The pooled OLS model and random-effects model yielded similar results in the sense that the adjusted R squared values indicated to both models explaining 8% of the dividend payout ratio. The results showed that board independence and previous dividend were negatively and statistically significant at 95% and 99% significance levels, respectively. Profitability and board ethnic diversity were positive and statistically significant, though at a lower confidence level of 90%. Gender diversity was positively related to dividends though it was statistically insignificant. Robustness checks using the percentage of women on the board as a gender diversity measure confirmed a positive and non-statistically significant relationship between gender diversity and dividend payout under both the pooled OLS model and the random-effects model. Furthermore, the direction of the coefficients remained consistent in all the independent variables.

Financial expertise has a negative and statistically insignificant relationship with dividend payout. Board size and average age of the board both have a positive and statistically insignificant relationship with dividend payout. To determine the reliability of the results produced by these two models, the study relies on the probability of the F-statistic, which is statistically significant at a 99% confidence level. This indicates that the results of the model can be relied on.

Based on the adjusted R squared value, the fixed effects model explains 10% of the dividend payout ratio. Similar to the pooled regression and random effects model, board independence and previous dividend are negatively and statistically significant at a 95% and 99% significance level. The p-values of board ethnic diversity and dividend payout indicate a positive and higher statistical significance than that found in the pooled OLS and random-effects model. Robustness checks using the percentage of women on the board as a diversity measure also confirm a positive and non-statistically significant relationship between gender diversity and dividend payout.

Similar to the results above, the fixed effects model shows that financial expertise has a negative relationship with dividend payout, though statistically insignificant. Board size and the average age of the board both have a positive and statistically insignificant relationship

with dividend payout. The probability of the F-statistic is statistically significant at a 95% confidence level, which indicates that the results of this model can be relied on, albeit at a lower confidence level than that of the pooled OLS and fixed effects regression.

The Hausman test was conducted to determine the preferred model between the random effects regression and the fixed effects regression. The results showed a p-value of 0.00 and, accordingly, the hypothesis that the random effects model is the most appropriate model is rejected and the fixed effects model is chosen as the alternative.

To determine the most appropriate model between the fixed effects model and the pooled OLS model, a redundant fixed effects test was performed. The results showed that the null hypothesis of redundant fixed effects can be accepted using p-values of both the cross section (0.30) and cross sectional Chi Square (0.13) which are both greater than 0.05. This means that the intercept is constant across all variables and there is no need to account for heterogeneity hence the pooled OLS regression is the preferred model. Accordingly, the results from the pooled OLS are interpreted.

5.5.2 Hypotheses testing outcomes for the study

Before engaging in a detailed discussion of the results obtained from the preferred model (pooled OLS), the following table reconciles the formulated hypotheses for the study with the regression outcomes. Hypotheses were either accepted or rejected based on the statistical significance of the results.

	Hypothesis	Accepted/Rejected
H_1	There is a relationship between gender diversity and dividend payout	Rejected
H_2	There is a relationship between ethnic diversity and dividend payout	Accepted
H_3	There is a no relationship between ethnic diversity and board and dividend payout	Rejected
H_4	There is a relationship between average age of board members and dividend payout	Rejected
H_5	There is no relationship between average age of board members and dividend payout	Accepted
H_6	There is a relationship between financial expertise and dividend payout	Rejected
H_7	There is a relationship between board size and dividend payout	Rejected
H_8	There is a negative relationship between board independence and dividend payout	Accepted
H_9	There is a positive relationship between profitability and dividend payout	Accepted
H_{10}	There is a relationship between previous dividend and dividend payout	Accepted

Table 5.12: Hypotheses outcomes

Source: Author's own construction

5.6 DISCUSSION OF FINDINGS

The pooled OLS model reflects an adjusted R squared of 8%, which means the model explains only 8% of the dependant variable, leaving other factors to account for the remaining 92%. Brooks (2013) holds 35% to be the benchmark for a model that is capable of explaining relationships under study.

However, Grace-Martin (2012) and Itaoka (2012) agree that it is common for studies using demographic explanatory variables to experience models with low R squared values. The evidence of their assertions can be found in some studies using demographic variables (Dolamo, 2017; Khan et al., 2017; Taylor & Peens, 2017). However, they hold that it should not be deemed inappropriate or impossible for meaningful insights to be derived from these models. They concur that models with low R squared values can be relied on if the purpose of the research is to establish relationships rather than for predictions (for example GARCH modelling). Against this background, it is deemed appropriate to interpret results from the pooled OLS regression since this work seeks to ascertain relationships between select board characteristics and dividend payout.

First, the study acknowledges that it is not common practice to discuss non-statistically significant results. However, this study can be viewed as a starting point for studies seeking to determine the relationships between board diversity and dividend payout. Furthermore, a major contribution of this study is to the ongoing debate on whether gender diversity quotas could improve organisational outcomes. Therefore, this study views a discourse on the insignificant gender diversity results to be a necessity.

The results in **Table 5.11** show that there is a positive relationship between gender diversity and dividend payout. The direction of the relationship is expected as it supports the agency perspective, which posits that gender-diverse boards are more inclined to pay higher dividends due to increased monitoring by female directors (Ye et al., 2019).

However, this result is statistically insignificant and similar to that obtained by Eluyela et al. (2019) who found that gender diversity does not have a significant influence on dividend payout amongst Nigerian firms. Similarly, these can be compared to results found by Taylor and Peens (2017) who found an insignificant relationship between gender diversity and firm performance in South African firms. These results suggest that the increased presence of

women serving on South African boards does not significantly affect firm performance or monitoring activities.

As expected, there is a positive and significant relationship between ethnic diversity and dividend payout. This is in line with previous literature (Al-Dhamari et al., 2016; Byoun et al., 2016). These studies agree that diverse boards pay larger dividends due to the enhancement of monitoring activities for the benefit of shareholders. This is in line with the agency theory perspective and the view that diverse cultures bring unique perspectives to the board. Therefore, ethnic diversity enhances monitoring activities (Al-Dhamari et al., 2016).

The results showing a negative and significant result between board independence and dividend payout are not surprising. Previous studies examining this relationship have found evidence supporting the substitution hypothesis (Abor & Fiador, 2013; Elmagrhi et al., 2017). The position is that firms with high independence have no reason to use dividends as a monitoring device. Instead, as board independence increases, the level of dividends decreases as funds are retained for future investment. This view is supported by Papo (2016), who also found a negative and statistically significant relationship between board independence and dividend payout within the South African context.

Table 5.11 shows that profitability has a positive and significant relationship with dividend payment, however at a much lower confidence level of 90%. While this confirms the findings by Firer et al. (2008), Fusire (2018) and Nyere and Wesson (2019) who studied this relationship in a South African context, the level of significance suggests that current profitability does not have as much impact as the previous dividend in explaining current dividend payout.

Table 5.11 shows that the relationship between the previous dividend and dividend payout can be explained at a 99 % confidence level. The negative direction of the relationship between the previous dividend and dividend payout was not expected. Figure 5.1 showed volatility in the dividend payout ratio between 2015 and 2018. A period of the high dividend was followed by a lower dividend for a few years before finally returning to a 'normal' dividend ratio. **(See Fig 5.1.)** This may explain the negative relationship, which is in contrast with findings by Dickens et al. (2002) and Imran (2011) who found a positive relationship between the variables.

In line with previous studies, there is strong evidence to suggest that ultimately, South African firms in the JSE top 40 aim to maintain stable dividends over time (Firer, 2008; Firer et al., 2008; Firer et al., 2013; Sibanda, 2016). Therefore, previous dividends are a massive

consideration in determining current year dividends. This is in line with Lintner (1956) who maintains that current profitability was not a strong base for the determination. Instead, managers aimed to smooth dividends over time.

5.7 SUMMARY

In this chapter, the relationship between dividend payout (DPR) and select board characteristics was analysed. The independent variables used in the study were board gender diversity (BGEN), board ethnic diversity (BETHN), financial expertise (FINEX), the average age of board members (AVAGE), board size (BSIZE), board independence (BIND), previous dividend (PREVDIV) and profitability (PROF).

Using 29 companies sampled from the JSE top 40 listed companies, three-panel models were applied to determine the relationship between the dependent variable and the independent variables. Results from the redundant fixed effect tests and Hausman tests determined the pooled OLS model to be the most appropriate model for interpretation.

The results showed evidence supporting the agency, resource dependence, maturity and dividend smoothing theories. Board ethnicity, board independence, previous dividend and profitability showed significant relationships with the dependant variable. However, there was no evidence to support that board gender diversity, financial expertise, average age of the board and board size have any significant relationship with dividend payout. Below, the final chapter summarises and concludes the study.

Chapter 6 Summary, Conclusions and Recommendations

6.1 INTRODUCTION

This study examined the relationship between select board characteristics and dividend payout in the JSE top 40 listed companies between 2013 and 2018. The independent variables of interest were the board demographic variables (gender diversity, ethnic diversity, the average age of board members and financial expertise). However, to reduce potential omitted variable bias, additional variables were employed as control variables (board independence, board size, profitability and previous dividend). The study is summarised here.

Chapter one provided a brief introduction and background to the research questions. **Chapters two and three** reviewed both the theoretical and empirical literature about this work. Specifically, chapter two discussed corporate governance theories but maintained a focus on their perspectives towards the role of the board. The theories discussed were the agency, stakeholder, stewardship, resource dependence and resource based view theories. The resource dependence and resource based view emphasised the importance of board diversity in enhancing corporate decision making and maximising shareholder value. In addition, the chapter discussed corporate governance developments in the UK, USA and South Africa.

Chapter three discussed the major dividend theories and presented the different positions of these on the relevance of dividends. Furthermore, the empirical literature was assessed to obtain an understanding of the factors that determine dividends, both from a global and from the South African perspective. This chapter discussed findings from extant literature on corporate governance and dividend payout.

It was discovered that the relationship between corporate governance and dividend payout remains under-researched. A higher proportion of the existing literature has examined the relationship between accounting-based variables (profitability, leverage, free cash flow, firm size) and dividend payout. Furthermore, the findings of the extant literature were conflicted. Others supported the view that companies with substantial shareholder rights paid dividends more generously than firms with fragile corporate governance standards (outcome view). Others supported the view that firms with weaker governance structures were more generous

with dividends as managers voluntarily offered payouts to compensate for the inherent weaknesses (substitute view).

Finally, the review of the literature showed that limited South African research on corporate governance and dividend payout has only investigated this relationship using structural variables, such as board size and board independence. The implication of this is that the influence of board demographic variables on South African dividends is unknown. This is despite growing global interest in understanding the relationship between board diversity and various organisational outcomes such as dividend payout and firm performance. Furthermore, South African firms are still transforming into diverse boards. This provides a compelling motivation for investors, policymakers and businesspersons to understand the relationship between board diversity various organisational outcomes.

These research gaps supported the need to undertake the study. However, it should be noted that the main contribution of this study to the existing body of knowledge is the introduction of a wider variety of variables, namely gender diversity, ethnic diversity, age diversity and financial expertise to studies examining the relationship between corporate governance and dividend payout in South Africa. This chapter was concluded with the formulation of ten research hypotheses and a presentation of this study's conceptual framework.

Chapter four presented the research methodology followed to answer the research questions. The main research question was, 'could relationships between additional characteristics of boards of directors and the dividend payout in the top 40 JSE Listed companies be established? The study adopted a quantitative research approach using panel regression as the primary method of analysis. Data was collected from EquityRT, IRESS and audited integrated annual reports. The final sample included 29 companies and the data for analysis spanned from 2013 to 2018, with a total 174 observations. All three-panel data models were considered to account for weaknesses inherent in each model. The Hausman test and Redundant Fixed Effects test were used as diagnostic tools to determine the preferred model for interpretation. The results from these tests revealed that the pooled OLS model was the best model for interpretation.

Chapter five presented the results and analysis of data. The results from the descriptive statistics were discussed, and time series plots were used to analyse trends in the data. In summary, the descriptive statistics confirmed that historically disadvantaged groups were still underrepresented in South African boards. It was interesting to discover that JSE top 40

directors are much younger than American boards, with the average age of board of members ranging from 54 to 57 years of age over the period of study. This is different to American boardrooms, where there are more directors above the age of 75 than those below the age of 50 (McGregor, 2018).

Five out of the ten hypotheses were rejected. No significant relationships were found between, on one hand, gender diversity, financial expertise, the average age of the board, board size, and on the other the dependent variable, dividend payout. This is in line with other researchers who found insignificant relationships between these variables and dividend payout.

In line with previous research, the results showed a significant relationship between ethnic diversity and dividend payout (Al-Dhamari et al., 2016; Byoun et al., 2016). However, this relationship was only significant at a 90% confidence level. As expected, board independence had a negative relationship with dividend payout. This relationship was highly significant. These results are supported by previous research, which yielded similar results.

The relationship between dividend payout and control variables, profitability and previous dividend, showed support of the maturity and dividend smoothing theories. This is in line with previous research that found that previous dividend was an important factor in determining the current dividend.

6.2 SUMMARY OF FINDINGS

6.2.1 Findings from descriptive statistics

There were two major findings from the descriptive statistics. First, there is large variation in female board representation within the sample during the observed period. In some companies, there was 0% female representation, while in others, females occupied 50% of the total board size. The results showed that there had been steady increases in female representation on South African boards. However, women remain underrepresented, mainly at an average of 20.4%. This is very low when compared to FTSE 100 companies that have an average of 32.1% female representation on their boards (Tobin, 2019). This suggests that there are still obstacles to the participation of women in South African boards.

A similar picture is demonstrated by the descriptive statistics on board ethnic diversity. The results indicate that the average percentage of Black people serving at company boards is 36%. This is quite alarming given that Black people make up 92.1% of the population (StatsSA, 2019).

The results reveal that percentage increases in gender and ethnic diversity have been slightly higher since the introduction of the King IV Report (2016). This could be an indication that companies are responding to calls for inclusivity by the King IV Report. However, the progress is slow and there is need for more considerable transformation efforts by JSE companies and policymakers.

6.2.2 Findings from the regression analysis

The regression analysis found significant relationships in four out of the eight independent variables, namely board ethnicity, board independence, profitability and previous dividend. The study expected to find a significant positive relationship between gender diversity and dividend payout. This was based on previous findings that women display greater commitment in fighting agency problems, and hence would improve monitoring by motivating for higher dividend payments. The results showed a positive relationship between gender diversity and dividend payout. However, the results indicated that the increased presence of women in boards was not significant in determining dividend payout and hence monitoring decisions in JSE top 40 firms. When these results are viewed in other South African studies that have found insignificant relationships with financial performance, it raises the question of 'tokenism' on South African boards (Dolamo, 2017; Taylor & Peens, 2017).

There is a danger that some companies may seek to appoint women as part of a 'tick box' exercise without expecting them to have a voice in important decisions. The probability of 'tokenism' is high because South African black women are historically disadvantaged from two standpoints, namely a gender perspective and a racial perspective. This places them at high risk for being used as 'symbols' in South African boards. However, 'tokenism' is very dangerous for corporates because the envisaged benefits of enhanced monitoring and decision making are not realised.

Another explanation of the insignificant relationship lies in the socialisation process following female board appointments. It is possible that existing male board members with traditional views on how the company should be run are resistant to suggestions brought in by new diversity appointments. As a response, female board members may feel the pressure to adopt the behaviour and norms of existing board members in order to feel accepted. In this regard,

the benefits of having female board members are forfeited and are therefore not recognisable in corporate decisions.

The positive relationship between board ethnic diversity and dividend payout was as expected, though it was not highly significant. Diverse directors bring unique cultural perspectives to the board. This is believed to enhance decision-making and improve monitoring functions. The result is in line with previous studies that found that boards with greater racial diversity use dividends as a conflict resolution tool between managers and shareholders. However, according to Byoun et al. (2017) and Al-Dhamari et al. (2016), this relationship holds in companies that already have agency problems.

The relationship between board independence and dividend payout was found to be more significant than that between ethnic diversity and dividend payout. From a South African perspective, the King IV (2016) emphasises the need for and value of independence on boards. In the UK, the various corporate governance codes also encourage board independence. (Examples are the Cadbury Report of 1992 and the Combined Code of 2010.) In this regard, companies incorporate board independence as a strong corporate governance mechanism, reducing the need to use high dividends as a monitoring device. There is stronger evidence to suggest that South African firms use dividends as substitutes for corporate governance mechanisms.

Two control variables, profitability and previous dividend were used to reduce potential omitted variable bias. The results revealed a positive and significant relationship between profitability and dividend payout. This is in line with the maturity hypothesis, which posits that mature, profitable firms are more likely to issue dividends (De Angelo et al., 2006). A significant number of companies in the JSE top 40 are inherently mature and stable; hence, they are in a better position to issue out dividends.

However, the highly significant relationship between the previous dividend and dividend payout suggests that firms consider the previous dividend in determining the current dividend payout. This is in line with the views shared by Lintner (1956), who maintains that managers aim to maintain a targeted ratio and therefore strive to smooth out dividends over time. The time series plots revealed some instability in dividend DPR in some years during the study.

It was interesting to note that during these years, a period of high dividends was followed by a period of low dividends until the DPR returned to the normal industry average. This is an indication that there were other factors that caused fluctuations in DPR, but companies

attempted to manage shareholders' expectations by alternating the level of dividends until they returned to the normal average. The dividend smoothing model is supported by other studies that have found evidence in dividend smoothing in South African companies. This suggests that the dividend behavior of companies in the sample behaves in a manner similar to those on the New York Stock Exchange and the Borsa Instabul (Bostanci, Kadioglu & Sayilgan, 2018).

6.3 IMPLICATIONS OF THE STUDY

First, the significant relationships between the two board characteristics confirmed that there is a relationship between board characteristics and dividend payout. The study advances the argument that for companies in the study sample, dividends act as substitutes for corporate governance mechanisms. It is the study's view that boards with diverse directors motivate high dividends in companies already facing agency problems. This is done to maintain relationships with existing shareholders. However, as independence increases, the need to use dividends as governance mechanisms reduce. Therefore, shareholders should note that firms with more independent directors are in a better position to retain funds for investment in future lucrative investment projects.

Second, the regression results do not provide a compelling business case for demographic diversity in boards, given that only one out of the four diversity measures showed a significant relationship with dividend payout. However, the descriptive statistics showed that there is need for more considerable transformation efforts in the JSE sectors, both in terms of gender and racial diversity. Against this background, the study views it necessary for policymakers to set legislative quotas similar to those found in Norway, Spain and France. Even so, the enforcement of these quotas needs to be supported by guidelines and processes that ensure that the efforts of transformation are not undermined. Naturally, the declining number of male directors during the observed period indicate that there are increased efforts to accommodate women on boards. However, caution needs to be exercised in ensuring that black men are not overlooked, given that companies might find it more convenient to appoint a single black female director to tick both the gender and racial diversity 'box.'

The study holds that appointing diverse directors in terms of gender, race, age and expertise is a step in the right direction. However, it urges companies to comprehend that the value of true diversity is found in the unique perspectives that enhance decision-making. Therefore, in addition to adopting legislation quotas, companies need to set policies that ensure that existing

directors are receptive of the views and contributions of new diverse appointments. Furthermore, companies must have a socialisation process that welcomes and empowers directors from historically disadvantaged backgrounds. This process must be transparent, backed up by company policy and should flow through the culture of the organisation. This commitment to inclusivity will reduce 'tokenism' and the presence of women and black directors may begin to show significance in financial performance and decision making.

6.4 LIMITATIONS AND RECOMMENDATIONS FOR FUTURE RESEARCH

The majority of the board diversity variables had insignificant relationships. Carrying out the research on a larger sample could have yielded different results. Data from only 29 companies were analysed in the regression. Therefore, it is envisaged that conducting similar research with a much larger sample could provide better insights on the relationship between board characteristics and dividend payout.

Similar to this study, a majority of studies examining the relationship between various factors and dividend payout focus on the larger JSE listed companies. Little is known about the determinants of dividend payout on smaller listed companies and SMEs. It would be essential to know the relationship, if any, that exists between corporate governance and dividend payout in smaller South African firms.

Although some useful insights were drawn from the regression, the explanatory power of the model was low. This study could be replicated using more advanced measures of diversity. This might have the added benefit of improving the explanatory power of the model.

Furthermore, insignificant relationships found in the majority of diversity variables may indicate that diversity is not about numbers but more about the diverse contributions shared in decision-making. This study used secondary data to measure variables such as board diversity and dividend payout. Future research could use interviews and qualitative analysis to determine whether there is a relationship between diversity and dividend payout.

6.5 CONCLUSION

The study posed the following question; could relationships between additional characteristics of boards of directors and dividend payout in the top 40 JSE Listed companies be established? In response, only one out of the four additional variables had a statistically significant

relationship with dividend payout. It is clear that there is no relationship between gender diversity, age diversity and financial expertise. Based on the outcome and substitute model of dividends brought forward by La Porta et al. (2000), this study found stronger evidence of the substitute model where dividend payouts are less pronounced in firms with stronger governance. Furthermore, the relationships found between profitability, previous dividend and dividend payout support the maturity and dividend smoothing theories for firms in the JSE top 40.



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Appendix 1 JSE top 40 companies in the final sample

	Name of Company
1	NASPERS LIMITED
2	ANGLO AMERICAN PLATINUM LIMITED
3	VODACOM GROUP LIMITED
4	FIRSTRAND LIMITED
5	STANDARD BANK GROUP LIMITED
6	KUMBA IRON ORE LIMITED
7	SANLAM LIMITED
8	CAPITEC BANK HOLDINGS LIMITED
9	MTN GROUP LIMITED
10	REMGRO LIMITED
11	RMB HOLDINGS LIMITED
12	ABSA GROUP LIMITED
13	ASPEN PHARMACARE HOLDINGS LIMITED
14	SHOPRITE HOLDINGS LIMITED
15	DISCOVERY LIMITED
16	OLD MUTUAL LIMITED
17	CLICKS GROUP LIMITED
18	SASOL LIMITED
19	THE BIDVEST GROUP LIMITED
20	NEDBANK GROUP LIMITED
21	GROWTHPOINT PROPERTIES LIMITED
22	RAND MERCHANT INVESTMENT HOLDINGS LIMITED
23	PSG GROUP LIMITED
24	TIGER BRANDS LIMITED
25	THE SPAR GROUP LIMITED
26	MR PRICE GROUP LIMITED
27	AFRICAN RAINBOW MINERALS LIMITED
28	WOOLWORTHS HOLDINGS LIMITED
29	SANTAM LIMITED

Appendix 2 Ethical Clearance

CBREC and SUBCOMMITTEES 2020



SCHOOL OF ACCOUNTING RESEARCH ETHICS COMMITTEE

Dear Ms Nhoro

ETHICAL APPROVAL GRANTED FOR RESEARCH PROJECT

Decision: Clearance granted

This letter serves to confirm that the proposed research project indicated in the table below, has been reviewed by the School of Accounting Research Ethics Committee (SAREC) at the University of Johannesburg. Ethical clearance is granted for 5 years, from 28 July 2020 to 31 July 2025.

Applicant	Tatenda Nhoro
Supervisor	Mrs M Hlobo & Prof T Moloi
Student number	217085800
Title of Research	Board characteristics and dividend payout in the top 40 JSE listed companies
Decision date	28 July 2020
Reviewers	M Bornman
Ethical clearance code	SAREC20200728/06
Rating of application	CODE 01

CODE 01 - Approved
CODE 02 - Approved with suggestions without re-submission
CODE 03 - Referred back
CODE 04 - Disapproved, cannot re-submit

The researcher/s may now commence with the study providing that:

1. The researcher will ensure that the project adheres to ethical research requirements;
2. The researcher will be conducting the study as set out in the approval application;
3. The researcher will ensure that the project adheres to all applicable legislation, scopes of practice, professional codes of conduct and scientific standards as it pertains to the field or study;
4. The researcher will bring to the attention of the research ethics committee any proposed changes, concerns that arise, and unexpected ethical management issues;
5. Any changes that can affect the study-related risks for participants or researchers must be reported to the committee in writing;

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CBREC and SUBCOMMITTEES 2020

6. All relevant permission required to access data, organisations, etc. has been obtained (where applicable);
7. No fieldwork activities may continue after the ethical clearance has expired. A request for an extension of ethical clearance can be made in writing to SAREC.

Prof M Bornman

Chairperson: SAREC

Email: mbornman@uj.ac.za

Telephone: 011 559 3873

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Appendix 3 Extract of Turnitin Similarity Report

23/10/2020

Turnitin

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The Relationship between Board Characteristics and Dividend

11

Payment in JSE Top 40 Listed Companies by TATENDA NHARO (217085800)

"MINOR DISSERTATION submitted in partial fulfilment of the requirements for the degree MAGISTER COMMERCII in FINANCE in the COLLEGE OF BUSINESS AND ECONOMICS at the UNIVERSITY OF JOHANNESBURG SUPERVISOR: Prof

3

Tankiso Moloi CO-SUPERVISOR: Ms Modi Hlobo {2020}" Acknowledgements My academic journey has not been an easy one.

I would not have been able to make it this far without the unwavering support of

200

those around me. First,

I would like to give thanks and praise to God for giving me the

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courage to keep going, especially during the most challenging times of this work. His promises held true as he continuously renewed my strength, guided my path and made certain that I was never alone. Selah! I am privileged to have had Professor Tankiso Moloi and Ms Modi Hlobo as my supervisors. They provided me with timely feedback throughout the writing process. Their work ethic and willingness to provide guidance made this daunting process an enjoyable one. I am forever grateful.

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