

# Investigating the link between board independence and dividend distributions in South Africa



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## Dates:

Received: 25 Sept. 2022  
 Accepted: 12 Jan. 2023  
 Published: 20 Feb. 2023

## How to cite this article:

Viviers, S., Mans-Kemp, N., Janse van Vuuren, M., & Shiel, T. (2023). Investigating the link between board independence and dividend distributions in South Africa. *South African Journal of Business Management*, 54(1), a3643. <https://doi.org/10.4102/sajbm.v54i1.3643>

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**Purpose:** As shareholder-elected monitors, independent non-executive directors (INEDs) should ensure that managers do not retain earnings to promote their own interests. The relationship between board independence and dividend distributions was hence investigated for selected companies listed on the Johannesburg Stock Exchange (JSE). The country offers a well-developed corporate governance framework to listed companies.

**Design/methodology/approach:** Data on the considered companies' dividend payout ratios (DPRs), board independence and six control variables were obtained from Bloomberg for the period 2007–2021. The significance of the observed trends in these variables was considered by conducting analysis of variance (ANOVA) and Fisher's least significant difference (LSD) tests. The hypothesised relationship was assessed using a mixed-model regression.

**Findings/results:** The results are in line with prior research showing that dividends are often omitted or reduced during and after crisis periods, that is, the global financial crisis (2008/2009) and the coronavirus disease 2019 (COVID-19) pandemic (2020/2021). A negative but statistically insignificant relationship was reported between DPR and board independence.

**Practical implications:** Although board independence was not significantly related to dividend distributions for the sampled companies, INEDs still perform an important monitoring role. Shareholders are thus encouraged to play a more active role in the election of these directors.

**Originality/value:** This study extends and refines previous research in South Africa and reveals new insights regarding board independence and dividend distributions during three King regimes and distribution-related regulatory changes.

**Keywords:** board independence; independent non-executive directors; King IV; dividend payers; dividend payout ratios; over-retention of earnings; resource dependence theory; agency theory.

## Introduction

'The harder we look at the dividend picture, the more it seems like a puzzle, with pieces that just don't fit together'. This quote by the renowned American economist Fischer Black (1976) gave rise to a substantial body of research on the dividend distribution decision in the decades that followed (e.g. Al-Najjar & Kilincarslan, 2019; Baker et al., 2002; Frankfurter, 1999). Researchers have investigated a wide range of factors that could influence the distribution of a company's earnings, including various internal and external corporate governance mechanisms (Abor & Fiador, 2013; Adjaoud & Ben-Amar, 2010; Benjamin & Zain, 2015; Briano-Turrent et al., 2020; Mehdi et al., 2017; Mitton, 2004; O'Connor, 2013; Sanan, 2019; Sharma, 2011).

Several international scholars have investigated the relationship between a company's dividend distributions and the independence of its board, an important internal corporate governance mechanism (Al-Najjar & Hussainey, 2009; Benjamin & Zain, 2015; Mehdi et al., 2017; Sharma, 2011). According to the resource dependence theory, independent non-executive directors (INEDs) bring valuable resources to the boardroom (Johnson et al., 1996). By providing access to key constituents such as buyers, suppliers, social groups and policymakers, these unaffiliated or outside directors as they are also called, not only enhance a board's functioning but also contribute to a company's legitimacy (Hillman et al., 2000).

INEDs furthermore provide valuable skills and experience and perform a critical role in monitoring managers' actions (Abor & Fiador, 2013; Bonazzi & Islam, 2007; Fama & Jensen, 1983; Nguyen et al., 2017; Sharma, 2011). The agency theory posits that effective monitoring will prevent managers from promoting their own interests at the expense of shareholders (De Andres & Vallelado, 2008; Jensen, 1988). The over-retention of earnings can lead to managers building empires and investing in projects with negative net present values (Stulz, 1990). Both self-promoting actions by managers can destroy shareholder wealth and increase agency costs.

As in many international studies (Briano-Turrent et al., 2020; Mitton, 2004; Sawicki, 2009), local scholars Mans-Kemp and Viviers (2015) also included board independence in a comprehensive corporate governance scorecard applied to companies listed on the Johannesburg Stock Exchange (JSE). These authors reported a positive, albeit insignificant, relationship between the sampled companies' corporate governance scores and dividend payout ratios (DPRs) over the period 2002–2010. A company's DPR reflects the percentage of attributable earnings that were distributed to ordinary shareholders in a particular year. The findings were interpreted in line with the outcome theory of dividends. This theory suggests that dividends are the outcome of an effective governance system (La Porta et al., 2000). Using more recent data (2013–2018), Moloi et al. (2021) found a significant negative association between board independence and DPR for large (Top 40) JSE-listed companies. Their results provide evidence for the substitution theory. This theory posits that dividends and board independence act as substitutes for managerial monitoring (Grullon & Michaely, 2002). Similar results were reported by Aigbovo and Evbayiro-Osagie (2022) for publicly listed companies in South Africa, Nigeria and Kenya over the period 2007–2021.

South Africa presents an interesting research context, given the introduction of more stringent liquidity and solvency requirements relating to distributions in the *Companies Act (No. 71 of 2008)* and changes to the dividends tax regime in 2012. Furthermore, regulators have stressed the importance of good governance for almost three decades. Given the mixed empirical evidence, the authors investigated the association between board independence and dividend distributions for selected JSE-listed companies over a 15-year period that includes regulatory changes and two crisis periods, namely the global financial crisis (2008/2009) and the coronavirus disease 2019 (COVID-19) pandemic (2020/2021). Two research objectives were formulated. Firstly, to investigate the trends in the dividend distributions and the percentage of INEDs of selected JSE-listed companies over the period 2007–2021. Secondly, to explore the relationship between board independence and DPRs of the sampled companies over the research period.

This study is important from a corporate governance perspective, as the empirical evidence could be useful for managers and directors of JSE-listed companies. They should

ensure that dividend policies reflect recent developments in financial markets and shareholder preferences. Recommendations are furthermore offered to shareholders as their voting decisions can have substantial implications for director independence in South Africa, given the debate on factual versus perceptual independence (Deloitte, 2017a). Suggestions are also offered for future researchers to account for the distribution preferences of companies and shareholders in emerging versus developed markets.

The article is structured as follows: A brief overview of corporate governance in South Africa is presented next, followed by a discussion of earnings distributions in the country. The focus then turns to pertinent literature on the relationship between board independence and dividend distributions both locally and further afield to derive the hypothesis. A detailed discussion is then provided on the methods used to collect and analyse secondary quantitative data, whereafter key findings, conclusions and recommendations are provided.

## The corporate governance landscape in South Africa

The publication of the first King report in 1994 coincided with the first democratic election being held in the country (Institute of Directors South Africa [IoDSA], 1994). The principles underpinning sound corporate governance and practical guidance on the application thereof were revised and refined in 2002, 2009 and 2016 (IoDSA, 2002, 2009, 2016).

King II made specific reference to board roles, shareholder activism and the importance of an internal audit charter (IoDSA, 2002; Rademeyer & Holtzhausen, 2004). King III introduced more principles and was drafted on an 'apply or explain' basis. Companies that failed to apply certain principles should thus have explained their rationale for doing so (IoDSA, 2009). King IV requires companies to apply and explain their actions (IoDSA, 2016). The focus has thus shifted from merely disclosing which practices have been implemented to explaining the effect of those practices on stakeholders. Whereas King III and its predecessors arguably encouraged 'tick-box compliance', King IV was designed to promote the board's engagement with the 'spirit of the code' (Natesan & Du Plessis, 2019).

King IV states that a board (through its nomination committee) should determine whether its directors are independent in their judgement and character and whether there are circumstances or relationships that might affect, or appear to affect, their objectivity (Deloitte, 2017b). The practice of classifying INEDs has evolved from a list of disqualifying criteria in King III to a more perceptual approach that focuses more on the perception of independence than the practice thereof (Deloitte, 2017b).

The following criteria are used to categorise INEDs in South Africa (Erasmus & Le Riche, 2017): According to the

Companies Act, an independent director should not be involved in the daily management of company, should not have been employed as a full-time employee and/or prescribed officer during the previous three financial years and is not a material supplier and/or customer. Furthermore, King III and IV, *inter alia*, stipulate that an INED should not be a representative of a shareholder who can control or significantly influence corporate leaders, does not have a direct or indirect interest exceeding 5% of the company's shares, was not employed as an executive and/or designated auditor and/or legal advisor at the company for the preceding 3 years, is not an immediate family member of an executive, is free from any relationship that could interfere with their capacity to act independently, does not receive pay contingent upon corporate performance, is not a significant financial capital provider and does not participate in the company's share-based incentive scheme.

The presence of INEDs on a board is critical in ensuring that no individual or group of individuals yield unfettered power on the board (Bonazzi & Islam, 2007). King IV thus recommends that a governing body should comprise a majority of non-executive members, most of whom should be independent (IoDSA, 2016). The chairperson of the board should also be an INED. Specific guidelines further apply to the standing board committees. Whereas all members of the audit committee should be INEDs, most of the members of the risk, remuneration, nomination and social and ethics committees should be INEDs (IoDSA, 2016).

Scholars noted that INEDs tend to insist on more transparent reporting (Armstrong et al., 2014) and have been credited with generating higher returns for acquirers in merger and acquisition transactions (Wang et al., 2015). The increased independence of remuneration and audit committees has furthermore been associated with lower levels of earnings management and compensation paid to chief executive officers (CEOs) (Cornett et al., 2009).

According to Claessens and Yurtoglu (2013), the JSE's disclosure requirements are equal to or better than those of exchanges in several developed countries. Most of these requirements are aligned with the governance principles contained in the respective King reports. There are, however, notable cases where JSE-listed companies made comprehensive disclosures but still failed to demonstrate good governance. For example, Steinhoff International Holdings had several INEDs who served on its board and standing committees. Yet many of them had lengthy tenures and significant crossholdings that could have clouded their objectivity (Naudé et al., 2018).

Furthermore, despite the discussed King III and IV director independence guidelines (IoDSA, 2009, 2016), shareholder activists have long been frustrated with JSE-listed companies that classify board members from founding families, long-tenured and overboarded directors as INEDs (Viviers, 2016). The term overboardedness refers to directors who serve on

multiple boards concurrently (Harris & Shimizu, 2004). King IV's emphasis on a perceptual rather than a factual approach to classify INEDs arguably gives too much credence to the resources that they bring to the table relative to their monitoring function.

Ordinary dividends, special dividends and share repurchases are typically used to distribute earnings. The following section provides some background on these forms of earnings distribution among local companies.

## Earning distributions in South Africa

In line with trends in Europe (Andriosopoulos & Lasfer, 2015) and the Americas (Floyd et al., 2015), share repurchases have become increasingly popular in South Africa (Wesson & Botha, 2019; Wesson et al., 2017). Some companies favour share repurchases over cash dividends as the former facilitates capital structure changes and signals management's confidence in the company's prospects. Few researchers in South Africa have investigated the extent of share repurchases because of opaque company disclosures (Steenkamp & Wesson, 2020). Special dividends are typically paid in the wake of a large divestiture but could also be the result of a currency windfall or commodity boom. Special dividends are generally excluded from scientific studies as they are paid at random.

A longitudinal study among JSE-listed companies showed that the number of dividend paying companies (henceforth called payers) across nine industries and average DPRs decreased from 1977 to 2013 (Viviers et al., 2013). Before 01 April 2012, Secondary Tax on Companies (STC) was applicable in South Africa. This taxation was levied on local companies when they declared dividends (irrespective of the actual payment date). In contrast, dividends tax that replaced the STC in 2012 is levied on shareholders when they receive dividends. As such, dividends are only subject to dividend tax when they are declared and paid (South African Revenue Service, 2022).

Nyere and Wesson (2019) found that ordinary cash dividends by JSE-listed industrial companies increased over the period 1999–2014. These authors attributed the significant rise in dividends, which occurred after the global financial crisis, to regulatory reforms in the country at the time. Company size and profitability were positively associated with the sampled companies' DPRs, whereas negative relationships were reported with sales growth and free cash flow (FCF). Furthermore, Nel et al. (2021) observed that high ownership concentration was significantly related to lower ordinary dividends and capital distributions. Their sample included companies across three main industries, namely basic materials, industrials and financials.

## Overview of prior research and hypothesis development

Seminal corporate governance scholars argued that independent directors enhance monitoring of managerial

decisions (Fama & Jensen, 1983; Weisbach, 1988). One board decision that requires careful scrutiny by unaffiliated directors deals with the retention of the company's earnings. Agents might be tempted to retain these earnings to promote their own interests at the expense of shareholders (Jensen, 1988). Kasanen et al. (1996) argued that dividend policies and earnings management are connected. Earnings management occurs when accounting techniques are used to avoid earnings decreases and losses (Burgstahler & Dichev, 1997). Pressure to meet market expectations has been identified as one of the reasons for misrepresenting financial statements (Litt et al., 2014).

The same could be said of dividends that are employed to signal a company's financial health, even if its fundamentals portray a different message. Concerns regarding the use of dividends for window dressing purposes have been noted as far back as the 1970s (Bhattacharya, 1979). Effective monitoring by INEDs has been proposed to mitigate managerial efforts to mislead outsiders. Some empirical evidence for this proposition has been uncovered by scholars such as Chen et al. (2015) and Frankel et al. (2011).

In many studies, board independence is considered as one element of a composite governance score when investigating this variable's relationship with dividend distributions. Other board attributes include board size, gender diversity, chairperson-CEO role duality, director tenure, director overboardedness and the composition of audit, remuneration and nomination committees, as discussed in the remainder of this section.

Mitton (2004) used such a composite corporate governance score and determined that companies with higher scores, across 19 emerging markets, had higher DPRs. The positive relationship between corporate governance and dividend payouts was furthermore limited to countries with strong investor protection, including South Africa. Sawicki (2009) likewise used a composite corporate governance score and observed a positive relationship with dividend payouts. The study centred on evidence from Hong Kong, Indonesia, Malaysia, Singapore and Thailand before and after the Asian financial crisis (1999–2003).

The role of INEDs is even more pronounced during stressful periods, given the heightened need for expert advice to navigate crises (Jenwittayaroje & Jiraporn, 2019). More focus is accordingly placed on the optimal deployment of resources while accounting for potential agency conflicts to ensure corporate survival. The impact of sound corporate governance practices on corporate outcomes likewise receives more attention during crisis periods (Chintrakarn et al., 2021). While corporate leaders are likely to retain cash during challenging periods, several shareholders might prefer pay-outs, as the distribution decision is largely based on agents' and principals' divergent opportunity expectations and preferences (Lindén et al., 2022).

Most studies furthermore show that dividend distributions were higher in companies with greater board gender diversity

and larger boards (Abor & Fiador, 2013; Aigbovo & Evbayiro-Osagie, 2022; Briano-Turrent et al., 2020). Researchers explained this finding based on the agency theory that postulates that larger boards consist of more individuals to monitor and address opportunistic managerial behaviour (De Andres & Vallelado, 2008), including the over-retention of earnings (Abor & Fiador, 2013).

Using evidence from several emerging markets (Bahrain, Indonesia, Kuwait, Oman, Malaysia, Saudi Arabia, Thailand and Taiwan), Mehdi et al. (2017), however, noted an inverse relationship between boards size and dividend distribution. The study covered the 2008/2009 global financial crisis. Board size was deemed more relevant in the considered emerging markets during this crisis. Mehdi et al. (2017, p. 292) argued that companies with larger boards might have mitigated the use of dividends as a signal of performance during a crisis period, as the sizeable board acted as a 'credible signal' to the market. Dividend payouts furthermore tend to be lower in companies where the roles of the CEO and chairperson of the board are performed by the same individual (Briano-Turrent et al., 2020; Mehdi et al., 2017).

Sharma (2011) reported a positive association between the propensity to pay dividends and director tenure, and a negative link with busy directors. Directors holding more than three directorships at the same time are said to be overboarded and might struggle to perform their monitoring roles effectively (Weir et al., 2020). Sharma (2011) argued that the INEDs under investigation were conscious of shareholder activism and realised the importance of promoting shareholders' interests through the payment of cash dividends to retain their board seats.

Benjamin and Zain (2015) hence included board meeting attendance alongside board independence as a potential determinant of dividend distributions. These authors found that companies with a higher proportion of independent directors and whose boards met more frequently paid lower dividends. The findings suggest that corporate governance and dividend payouts serve as substitutes to reduce agency costs.

In emerging markets where researchers focused exclusively on board independence as an internal corporate governance measure, most reported a negative relationship with dividend distributions (Benjamin & Zain, 2015; Boshnak, 2021; Mehdi et al., 2017). Al-Najjar and Hussainey (2009) also uncovered an inverse association between dividend payouts and the number of outside directors serving on the boards of 400 non-financial companies listed on the London Stock Exchange (LSE) from 1991 to 2002. These authors deemed dividend payouts and independent directors as alternatives to lower agency costs and hence argued that they can be seen as substitutes. In contrast, by using data for 944 companies listed on the New York Stock Exchange and National Association of Securities Dealers Automated Quotations (NASDAQ), Sharma (2011) found a positive association between the propensity to pay dividends and board independence.

Driver et al. (2020, p. 559) critiqued the agency-based notion that dividends 'keep managers honest' and mitigate the over-investment problem. Their study among LSE-listed companies showed little support for the traditional agency theory. Short-term investor pressure on companies was found to be much more important than investment opportunities in prompting dividend payments. Companies with a high percentage of INEDs had significantly higher DPRs.

The role of ownership structure and concentration also featured in some dividend distribution studies. Using data from listed companies in Brazil and Chile from 2004 to 2014, Briano-Turrent et al. (2020) determined that family-controlled companies distributed more dividends than their non-family-controlled counterparts. In contrast, family ownership and control through pyramid structures in Colombia resulted in fewer dividends being distributed annually (Gonzalez et al., 2014). Institutional ownership generally had a positive influence on dividend payments (Abor & Fiador, 2013; Mehdi et al., 2017).

Prior studies featuring South Africa warrant closer attention. Using a composite governance score, Abor and Fiador (2013) established that good corporate governance led to high dividend payouts in South Africa, Kenya and Ghana from 1997 to 2006. The positive association was possibly because of easy access to and the low cost of external finance. Mans-Kemp and Viviers (2015) likewise reported a positive, albeit statistically insignificant, relationship between a composite corporate governance score and DPR. This study was conducted for a sample of JSE-listed companies over the period 2002–2010 (King II regime).

More recently, Aigbovo and Evbayiro-Osagie (2022) investigated the relationship between board independence and dividend distributions in South Africa, Nigeria and Kenya from 2007 to 2021. These authors found that board independence had a significant negative influence on dividend payouts, whereas board size, board gender diversity and management ownership all directly and materially affected the payouts of listed non-financial firms. The results of Aigbovo and Evbayiro-Osagie (2022) mirror those of Moloi et al. (2021) who also uncovered a significant negative association between board independence and DPRs over the period 2013–2018. In light of the extant literature, the following directional hypothesis was tested in this study: DPRs were inversely related to board independence among selected JSE-listed companies over the period 2007–2021.

In addition to the discussed earnings management and board size considerations, several other company-level factors have been shown to influence the relationship between board independence and dividend distributions. Commonly used control variables in distribution and director independence studies will now be shortly discussed. These include company size, board size, revenue growth, profitability and FCF.

Large companies are not only more prone to distribute earnings but also more likely to have higher DPRs than their

smaller counterparts (Adjaoud & Ben-Amar, 2010; Fatemi & Bildik, 2012; Grullon & Michaely, 2002). According to O'Connor (2013), the separation of ownership from control, which results in agency conflicts (and costs) between managers and minority shareholders, is more prevalent in large companies. By paying dividends, managers try to establish a reputation for the equitable treatment of current (and prospective shareholders), thereby reducing agency costs and improving access to reasonably priced external capital. DeAngelo et al. (2006) also note that larger companies tend to have fewer investment opportunities that require internal funding. As such, they are in a better position to distribute cash than their smaller counterparts.

Two opposing views exist regarding the effect of board size on dividend distributions. One school of thought supports the idea that larger boards allow managers to specialise, which is said to promote effective monitoring of managerial behaviour. Lower dividends are thus required to appease shareholders (Mehdi et al., 2017). Other scholars argue that larger boards are less effective than smaller boards owing to communication challenges. Larger boards thus feel more pressure to pay dividends as a means of convincing shareholders that effective monitoring is taking place, particularly as it relates to capital investments (Moloi et al., 2021).

Prior research, both in developed and emerging markets, shows that dividend payouts tend to be higher in companies that enjoy high levels of revenue (or sales) growth (Nyere & Wesson, 2019), those that are profitable (Aivazian et al., 2003; Fatemi & Bildik, 2012; Firer et al., 2008) and those that generate high levels of FCFs (Adjaoud & Ben-Amar, 2010; Grullon & Michaely, 2002; Sanan, 2019; Zhou & Ruland, 2006). As dividends are paid in cash, FCF is the most important of these three variables, especially during crisis periods (Forti & Schiozer, 2015).

Many authors use the operating profit margin, return on assets (ROA) and return on equity (ROE) as measures of profitability in dividend studies (e.g. Boshnak, 2021; Mehdi et al., 2017; Mitton, 2004; Sharma, 2011). As expected, Nyere and Wesson (2019) determined that company size and profitability were positively related to dividend distributions in South Africa.

## Research design and methodology

In this section, attention will be given to the population and sample description, operationalisation of the variables, data collection and analysis.

### Population and sample description

The population consisted of all companies that were listed on the JSE over the period 01 January 2007 to 31 December 2021. As indicated in Table 1, the population declined considerably over the research period. This trend is attributed to stringent regulatory and governance requirements, a weakening South African economy, and the

**TABLE 1:** Population and sample sizes per annum.

Year	Population size <sup>†</sup>	Sample size <sup>‡, §</sup>
2007	411	53
2008	411	76
2009	398	91
2010	397	112
2011	395	122
2012	387	118
2013	375	119
2014	380	121
2015	382	116
2016	376	115
2017	366	113
2018	360	118
2019	343	114
2020	331	104
2021	324	103

COVID-19, coronavirus disease 2019; JSE, Johannesburg Stock Exchange.

<sup>†</sup>, World Federation of Exchanges (2022); <sup>‡</sup>, Fortress Real Estate Investment Trust (REIT) Ltd had two tickers (FFA and FFB). As the data relating to the variables for the two tickers were the same, only data for one ticker (FFA) were retained; <sup>§</sup>, As a result of the COVID-19 pandemic, some JSE-listed companies approached the JSE (2020a) with requests to either cancel dividend payments, postpone payments or make changes to the value of the dividends that have previously been declared pursuant to the JSE corporate actions timetable. The JSE (2020b) only allowed companies to cancel a dividend and the resultant payment prior to the finalisation date. Observations of companies that subsequently reduced or deferred their dividends as a result of COVID-19 were included in the current sample for 2020. The JSE did not make a similar allowance in 2021.

relatively high costs of listing on the JSE (Kruger, 2022). Two criteria were used to select the sample:

- Companies had to have listed ordinary and/or N-class shares and
- Companies had to have dividend and board independence data on Bloomberg for at least 1 year during the research period (2007–2021).

A company did not have to be listed for the full duration of the research period. Companies that delisted at any point during the research period were included in the non-probability sample to address survivorship bias for the period during which they were listed. Data were collected at the sampled companies' respective financial (reporting) year-ends. Companies could have a primary or secondary listing on the JSE. For dual listings, the limited (Ltd) and the public limited company (plc) companies were included in the sample if their dividend and board independence data differed. Examples include Mondi Ltd and Mondi plc and Investec Ltd and Investec plc.

Most of the sampled companies conducted business in the basic materials (22.26%) and financials (18.43%) industries followed by consumer staples (13.42%). An almost equal number of companies operated in the consumer discretionary industries (12.98%) and industrials (12.10%). Some real estate (9.87%), health care (4.08%), communication services (3.32%), information technology (3.26%) and energy companies (1.19%) also featured in the sample.

### Operationalisation of the variables

A range of measures can be used as proxies for dividend distributions. Most scholars use DPR either on its own (e.g. Aigbovo & Evbayiro-Osagie, 2022; Mans-Kemp &

Viviers, 2015; Moloi et al., 2021; O'Connor, 2013) or in combination with the propensity to pay a dividend (Al-Najjar & Hussainey, 2009). The propensity to pay a dividend was included in the descriptive analysis. In line with the majority of prior scholars, DPR was used as the dependent variable to empirically investigate the hypothesised relationship between dividend distributions and board independence.

Bloomberg defined DPR as the percentage of net income that a company paid to ordinary shareholders in the form of a cash dividend in a particular year. Net income was defined as income before extraordinary items less minority and preference dividends. A DPR of zero implies that a company retained all its earnings in a year. This situation typically occurs when a company faces financial distress or when earnings are withheld to finance new ventures (Ahmed, 2015).

A DPR of 100% implies that all earnings were distributed to shareholders in the form of a cash dividend. Such a distribution strategy is not sustainable in the long term as the company will not have any retained earnings to finance growth opportunities or to manage unexpected crises. Distributing more earnings than have been generated (DPR > 100%) must be financed from sources other than the company's operations and is therefore also unsustainable in the long run. None of the sampled companies had negative DPRs. A negative DPR can occur if a company reported a loss for the year, and either paid a dividend or refrained from paying one. Only ordinary cash dividends were considered. No scrip dividends or property dividends were examined.

Companies that had DPRs of zero were classified as non-payers and were assigned a score of zero (0). In contrast, companies with DPRs in excess of zero were regarded as payers and were given a score of one (1). These classifications were used to determine the percentage of dividend payers per year, that is, the number of dividend payers divided by the total number of companies in the sample in the particular year. This interval-scaled variable is denoted as %DivPayers in the descriptive results.

Details on the study's independent and six control variables are presented in Table 2. These variables were identified based on corporate governance and dividend studies conducted in South Africa and internationally, as discussed in the preceding overview of prior research and hypothesis development section. As with the DPR data, data on the independent and control variables were downloaded from the Bloomberg database at the sampled companies' respective financial year-ends. To ensure data accuracy, several cross-checks were conducted between the sampled companies' integrated reports and the data captured from the Bloomberg database.

### Descriptive and inferential analyses to address the first research objective

The first research objective, namely to investigate the trends in the dividend distributions and the percentage of INEDs of selected JSE-listed companies over the period

**TABLE 2:** Operationalisation of the independent and control variables.

Type of variable	Name of variable	Description
Independent	%INEDs <sup>†</sup>	The independent variable was measured by the percentage of INEDs serving on a company's board in a year. The variable is based on the company's own classification of directors as executive, NED or INED.
Control <sup>§</sup>	Company size <sup>†</sup>	Market capitalisation is typically used as a proxy for company size as market capitalisation can be measured at any point in time and is not affected by a company's industry classification (Dang et al., 2018; Zadeh & Eskandari, 2012). The sampled companies' market capitalisation values were captured at financial year-end in South African Rand. Bloomberg computed market capitalisation by multiplying the number of outstanding shares by the company's closing share price on the last trading day of the year. The number of outstanding shares excluded treasury shares. Given the presence of numerous outliers, this variable was winsorised.
	Board size <sup>†</sup>	The total number of full-time directors at financial year-end. Alternate directors were excluded.
	Revenue growth <sup>‡</sup>	The annual percentage change in accrued revenue as reported by the company.
	Operating profit margin <sup>‡</sup>	This ratio measures a company's pricing strategy and operating efficiency. Computed as operating income (or loss) divided by total revenue (multiplied by 100).
	FCF <sup>‡</sup>	Computed as operating cash flow minus capital expenditures. The computation for REITs was slightly different as property improvements were also subtracted from operating cash flow. Free cash flow represents the cash that a company can generate after allocating the required funding to maintain or expand its asset base.
	ROE <sup>‡</sup>	This measure of a company's profitability reveals how much profit a company generates with the money that shareholders have provided. Calculated as net income available for ordinary shareholders divided by average ordinary shareholders' equity (multiplied by 100). Return on equity was favoured over ROA in the current study as financial and mining companies formed part of the sample. The ROA metric is most useful to compare companies in the same industry, as companies operating in divergent industries use assets in different ways. For instance, banks tend to have significantly higher ROAs than more capital-intensive companies (Griff, 2014).

INEDs, independent non-executive directors; REITs, Real Estate Investment Trusts; ROA, return on assets; ROE, return on equity; FCF, free cash flow.

<sup>†</sup>, Ratio scale; <sup>‡</sup>, Interval scale; <sup>§</sup>, These variables were identified based on prior research (notably Abor & Fiador, 2013; Aivazian et al., 2003; Al-Najjar & Hussainey, 2009; Nyere & Wesson, 2019; Sanan, 2019).

2007–2021, was addressed by conducting descriptive statistics for %DivPayers, DPR and the percentage of INEDs. Measures of central tendency and dispersion were computed.

In addition, analysis of variance (ANOVA) was conducted to investigate significant differences over the entire study period. This special case of the linear regression model has three distinct features, namely that parameters are estimated by ordinary least squares, the *F*-test is used for hypothesis testing and betas are assumed to be fixed parameters (Demidenko, 2013).

When an ANOVA is performed and the *F*-test indicates a significant difference, the Fisher's least significant difference (LSD) test can be used to make pair-wise comparisons among sample means to assess between which years the significant differences occurred (Ott & Longnecker, 2010). This test was conducted to investigate changes in the discussed variables for the respective years under consideration.

### Mixed-model regression to address the second research objective

The hypothesised relationship between dividend distributions (DPR% was used as the dependent variable), and board independence (%INEDs) was investigated by conducting a mixed-model regression. Year and all other predictors were included as fixed effects. A first-order autoregression correlation structure was used to model the time-series component of the collected panel data.

Given the presence of outliers, some DPR values were winsorised. Winsorising was done using the inter-quartile range method as implemented in the scores function of the R outliers package. Multicollinearity was evaluated by calculating variance inflation factors (VIFs). As the highest VIF value was 2.58 (for year), followed by 2.07 for company size, all variables were included in the mixed-model regression.

## Empirical results

This discussion will commence with key findings related to the first research objective, namely to investigate trends in the dividend distributions and the percentage of INEDs over time. Thereafter, the results of the mixed-model regression that was conducted to address the second research objective will be outlined, namely to explore the relationship between board independence and the DPRs of the sample companies over the research period.

### The trends in the dividend distributions and the percentage of independent non-executive directors (first research objective)

Pertaining to the discussion of trends, the percentage of dividend payers will be firstly considered, followed by the DPR%. As indicated in Panel A in Table 3, the percentage of the sampled companies that paid dividends remained above 80% for the largest part of the study period. However, not only did fewer companies pay dividends in 2020 (the first year of the COVID-19 pandemic), but the average DPR in this year was also the third lowest of the entire research period (Panel B in Table 3). The average DPR in 2021 was even lower at a mere 37.77%. A similar picture emerged during and directly after the 2008/2009 global financial crisis for the sampled companies. Yet the observed trend in the average DPR was not significant over the research period ( $F [14, 1420] = 1.03, p = 0.42$ ).

These findings confirm previous research showing that dividends are often omitted or reduced during economic or financial crises (Bozos et al., 2011; Forti & Schiozer, 2015). As mentioned earlier, the STC tax regime in South Africa changed to a dividend withholding tax (DWT) regime on 01 April 2012 (Nel et al., 2021). No statistically significant changes, however, occurred from 2011 to 2012 or from 2012 to 2013 in either the percentage of dividend payers or the average DPRs. According to Kantor (2018), dividends of JSE-listed banks grew faster than earnings since

approximately 2000 while their DPRs declined consistently since the global financial crisis. The descriptive statistics for the independent variable are shown in Table 4.

Perusal of Table 4 shows that the average %INEDs increased notably over the period under review. The ANOVA indicated that this trend was significant ( $F [14, 1420] = 7.87$ ,  $p \leq 0.01$ ). This finding is in line with other researchers who investigated board independence in South Africa (Muniandy, 2022; Weir et al., 2020). The %INEDs in 2011 was furthermore significantly higher than in 2010 ( $p < 0.01$ ). This result might be partly attributed to the introduction of King III. Another significant increase in this variable occurred from 2019 to 2020 ( $p < 0.05$ ). The sampled companies might have appointed more INEDs in 2020 to access their skills and resources to deal with the consequences of the COVID-19 pandemic, lending some support for the resource dependence theory.

Attention was also given to differences between sectors. While only a few communication services paid dividends, this industry showed the highest DPR% on average

**TABLE 3:** Descriptive statistics for dividend distributions per annum.

Year	Panel A		Panel B: DPR (%)			
	N	%DivPayers	Mean	Standard deviation	Min	Max
2007	53	88.68	45.10	28.41	0	243.58
2008	76	90.79	43.17	26.94	0	2746.23
2009	91	87.91	44.62	28.05	0	3098.58
2010	112	89.29	46.28	28.54	0	165.93
2011	122	89.34	48.70	30.35	0	3064.55
2012	118	91.53	47.56	27.25	0	3064.55
2013	119	90.76	46.44	26.64	0	418.58
2014	121	92.56	49.00	28.39	0	731.73
2015	116	88.79	49.43	28.66	0	213.34
2016	115	87.83	51.13	29.46	0	726.93
2017	113	87.61	52.42	30.21	0	284.94
2018	118	84.75	54.36	33.32	0	1153.03
2019	114	85.09	54.50	35.40	0	1153.03
2020	104	71.15	41.38	37.29	0	1153.03
2021	103	67.96	37.77	36.61	0	432.66

DPRs, dividend payout ratios.

**TABLE 4:** Descriptive statistics for % independent non-executive directors.

Year	Mean	Standard deviation	Min	Max†
2007	52.94	15.69	27.27	90.91
2008	52.15	14.68	25.00	92.86
2009	52.96	14.81	22.22	90.91
2010	52.48	14.04	22.22	91.67
2011	55.83	14.41	22.22	92.31
2012	57.99	14.77	22.22	92.31
2013	59.43	14.54	18.18	92.86
2014	58.75	13.49	27.27	91.67
2015	60.01	13.27	27.27	90.91
2016	61.40	12.72	30.00	90.91
2017	62.53	13.13	27.27	90.00
2018	62.37	13.32	18.18	100
2019	63.45	14.26	18.18	91.67
2020	66.85	12.97	20.00	100
2021	66.74	13.24	20.00	100

†, The two companies whose entire boards consisted of INEDs were investment holding companies with no executive directors.

(see Table 5). In contrast, many financial companies, such as banks and insurance companies, paid dividends, albeit a smaller proportion of earnings. Companies in the basic materials industry generally had the most INEDs on their boards, followed by companies in the consumer discretionary and consumer staples industries, respectively.

### The relationship between dividend distributions (%) and board independence (%) (second research objective)

Although DPR was inversely associated with %INEDs, the observed relationship was not statistically significant (see Table 6). As such,  $H_1$  could not be supported. In contrast, two studies that used data for selected JSE-listed companies reported significant negative relationships between dividend distributions and board independence (Aigbovo & Evbayiro-Osagie, 2022; Moloji et al., 2021). Aigbovo and Evbayiro-Osagie (2022) accounted for the linkages between corporate governance elements and the dividend distribution of listed companies in South Africa, Nigeria and Kenya over the period 2007–2021. Moloji et al. (2021) explored the relationship between board characteristics and DPR for 29 large JSE-listed companies between 2013 and 2018.

A similar picture emerges in other countries (Al-Najjar & Hussainey, 2009; Benjamin & Zain, 2015; Boshnak, 2021; Mehdi et al., 2017). These scholars interpreted this inverse relationship as evidence for the substitution theory. This agency-based theory posits that dividends can act as a substitute for having a sufficient number of independent directors on a board.

**TABLE 5:** Descriptive statistics per industry.

Industry	%DivPayers	DPR (%)	%INEDs
Communication services	3.56	69.92	60.18
Consumer discretionary	12.06	44.27	62.52
Consumer staples	15.25	60.00	57.62
Energy	1.09	48.22	55.09
Financials	20.12	51.70	58.30
Health care	3.70	35.91	58.98
Industrials	11.91	37.29	54.98
Information technology	3.12	38.73	53.92
Basic materials	19.39	38.09	63.68
Real estate	9.80	65.67	58.10

DPR, dividend payout ratio; INEDs, independent non-executive directors.

**TABLE 6:** Mixed-model regression results.

Value†, ‡	Standard error	t	p	
Intercept	7.090	1.025	<b>6.920**</b>	<b>0.000</b>
I: %INEDs	-0.006	0.011	-0.548	0.584
C: Company size	0.000	0.000	0.410	0.682
C: Board size	0.091	0.051	1.775	0.076
C: Revenue growth	-0.002	0.002	-1.186	0.236
C: Operating profit margin	-0.003	0.003	-0.901	0.368
C: ROE	-0.006	0.004	-1.515	0.130
C: FCF	0.000	0.000	0.694	0.488

Variance explained by model: 0.30.

INEDs, independent non-executive directors; ROE, return on equity; FCF, free cash flow.

†, I, independent variable; C, control variable; ‡, Given the presence of outliers, some values were winsorised; \*, Significant at the 5% level; \*\*, Significant at the 1% level.

## Conclusions and recommendations

Several scholars have investigated the effectiveness of various external and internal corporate governance mechanisms to curb the agency problem, including appointing a majority of INEDs. These independent monitors should, *inter alia*, ensure that managers do not retain company earnings to promote their own interests. Given South Africa's well-developed corporate governance framework, the link between board independence and the DPRs of selected JSE-listed companies was investigated over the period 2007–2021.

The results show that the number of dividend payers and the average percentage of earnings distributed to shareholders of JSE-listed companies substantially decreased following the advent of the COVID-19 pandemic. The same applies to the 2008/2009 global financial crisis. Efforts to deal with the adverse consequences of the COVID-19 pandemic might explain why more INEDs were appointed to the sampled companies' boards in 2020 and 2021. The adverse consequences of this pandemic coupled with several notable corporate scandals in JSE-listed companies (e.g. Steinhoff International Holdings, Sasol, Tongaat Hulett and EOH) during this period may have alerted companies to the need to shore up their independent monitoring on board-related decisions.

Although board independence was negatively related to DPR, this association was not significant. It should be taken into account that many factors influence the payment of dividends in South Africa (Nel et al., 2021; Nyere & Wesson, 2019). Furthermore, King IV affords JSE-listed companies substantial flexibility to classify their directors as INEDs. By paying dividends, some of the sampled companies might have attempted to deflect shareholders' scrutiny of INEDs who had lengthy tenures and those who served on multiple boards concurrently. This possibility calls for further investigation. In line with Aigbovo and Evbayiro-Osagie (2022), it is suggested that market regulators should ensure that listed companies apply the corporate governance guidelines to limit market infractions, enhance stakeholder confidence and stimulate investment.

The managers of JSE-listed companies should ensure that dividend policies reflect recent developments in financial markets and shareholder preferences. As shareholders function in the 'middle ground' between internal and external corporate monitoring mechanisms (Gantchev, 2013, p. 610), they are important change agents. By insisting on improved board independence, shareholders stand to benefit from reduced agency costs, including those associated with the over-retention of earnings problem. In line with King IV's view that shareholders can serve as proxies for broader stakeholder interests (IoDSA, 2016), other stakeholders, such as suppliers, employees and customers can also benefit from more effective monitoring as red flags in the company's finances or operations could be raised earlier.

Shareholders are thus encouraged to place more pressure on nomination committees to ensure that INEDs are accurately

classified, especially when it comes to overboarded directors, board members with tenures exceeding the prescribed 9 years and family members serving on the board. Shareholder activists can promote change through private engagements and by opposing the election or re-election of INEDs whose objectivity might be questionable. They should insist on disclosures outlining INEDs' board commitments at other listed companies, unlisted companies, state-owned enterprises, professional bodies and industry associations to make informed voting and investment decisions. The reasons for classifying family members and long-tenured directors as INEDs should be sufficiently explained.

In the current study, companies were only included if their dividend and board independence data were available on Bloomberg in a particular year. Future scholars can investigate which corporate governance mechanisms besides board independence and board size might explain dividend distributions in the South African context and other emerging markets. Lagging the variables might furthermore provide useful insights to future scholars.

Researchers can also explore why companies choose not to pay dividends. The assumption of the substitution model that poorly governed companies are typically financially constrained and the view that their managers aim to establish a reputation of treating their shareholders fairly by declaring dividends (Grullon & Michaely, 2002) also warrant further investigation in emerging markets. Future scholars can compare investors' tax preferences in selected emerging and developed markets. The influence of herding, anchoring and the *status quo* bias on the dividend distribution decision could also be explored, especially at companies with many interlocked directors. Interviews could also be conducted with members of nomination committees to gain more insights into the application of King IV's perceptual approach to the classification of INEDs. Interviews could furthermore be conducted with buy-side investors to gauge how these investors perceive the application of King IV's perceptual approach and whether these investors use their own metrics to assess independence.

## Acknowledgements

The authors wish to thank the following individuals for their assistance with this project: Sandri Smit, Martin Kidd and Johann de Villiers.

## Competing interests

The author(s) declare that they have no financial or personal relationship(s) that may have inappropriately influenced them in writing this article.

## Authors' contributions

S.V. conceptualised, wrote, reviewed and edited the article. N.M-K. and M.J.V.V. contributed to writing, reviewing and

editing the article. T.S. contributed to reviewing and editing the article.

## Funding information

The author(s) received no financial support for the research, authorship, and/or publication of this article.

## Ethical considerations

Project is exempt from ethics review and clearance. Reviewed by the Research Ethics Committee: Social, Behavioural and Education Research (REC: SBE).

## Data availability

The data were downloaded from the Bloomberg database and are hence available in the public domain.

## Disclaimer

The views and opinions expressed in this article are those of the authors and do not necessarily reflect the official policy or position of any affiliated agency of the authors.

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