IDENTIFYING KEY DETERMINANTS OF EFFECTIVE BOARDS OF DIRECTORS - EVIDENCE FROM NAMIBIAN LISTED COMPANIES

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ABSTRACT

The business world, investment community, academics and the society at large have a great interest in Boards of directors. According to Cadbury (1999) this interest is comprehensible given the fact that boards of directors serve as a link between the shareholders, who provide capital, and management responsible for running the company. The focal point of corporate governance debate is the perception that the board of directors is the preserver of shareholders' interest (Dalton et al., 1998). To the contrary, boards are being criticized for failing to meet their governance functions. Large institutional investors put pressure on (incompetent) directors and have long demanded changes in the board structure and attributes reflecting the board's inner workings (Monks and Minow, 2001).

Keywords: Board effectiveness corporate governance, boards of directors.

INTRODUCTION

In this present day, the market place has become particularly challenging where good players must be organizations that operate on rule-based systems rather than on relationship-based ones. This highlights, the significance of corporate governance, both in private and public institutions. Formal and informal institutions together oversee the relationship between the management and all others who invest resources in corporations. These organizations include the country's securities laws, corporate laws, accounting rules, largely accepted business practices and prevailing business ethics (Oman, C., Fries, S., and Buiter, W., 2003). The institutions of corporate governance thus serve as a platform for regulating appropriate behaviour in any given economy. Shleifer and Vishny (1997) give description of corporate governance as ―the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment. John and Senbet (1998) give a more broad definition that corporate governance deals with mechanisms by which stakeholders of a corporation exercise control over corporate insiders and management such that their interests are preserved.

The topic of corporate governance has attracted a very important level of attention both in academic research and in practice. The scandals that occurred in big businesses such as Parmalat, Lehman Brothers and Enron have placed the corporate governance systems of modern corporations under close analysis. These scandals have led to the focus on the roles of audit committees and external auditors and board independence. At the center of these corporate governance reforms and enhancements is a common interest in the effectiveness of boards of directors.

Several suggestions have been made in the wake of corporate failures about how to enhance the governance of companies in order to rebuild trust. These corporate governance transformations focus primarily on the makeup and the working of the board (Van den Berghe and Levrau, 2004). The board of directors is seen as a vital player in governance of companies hence the need for a better understanding of how this body works. Many studies in these areas has been in developed countries and not much work has been done in the areas of corporate governance and board effectiveness in the emerging markets of Africa.

There is a need for further research to understand better, document and operationalize board variables and board effectiveness in Namibian context. This paper seeks to identify and examine the key factors that lead to effective boards of directors, which in turn impacts firm performance.

LITERATURE REVIEW

Many discussions on corporate governance involves boards of directors and emphasize their significance to the success of the organizations they govern. Issues of governance arise whenever ownership of an entity is separated from its management. Agency challenges still exist in the business world because the interests of firms 'owners and managers (agents) are usually contrary (Dalton et al., 2007: 1) and as such room potential for managerial mischief.

Board effectiveness is mainly concerned with "task" outcomes and occurs by fulfilling a role set (Nicholson and Kiel 2004). The approach is, however, still subject to considerable debate in literature. The roles of boards of directors are commonly classified as: control, service and strategic role (Zahra and Pearce, 1989).

With respect to the control role, the board of directors has a lawful duty to oversee the company's operations and monitor top management performance in order to protect shareholders' interests (Lorsch and Maclver, 1989). Empirical studies on boards of directors have to a large extent been driven by the question of how much the board can influence firm performance. Various researchers have examined the direct impact of different board attributes on firm performance. Using financial performance as a proxy, they have explored board's effectiveness in protecting shareholders' interests, but have mostly shown inconclusive results (Coles, et.al. 2001).

Studies on board effectiveness has mostly depended on classical theories of corporate governance, such as agency, stewardship and resource dependence theories (Finegold et al., 2007; John and Senbet, 1998; Kiel and Nicholson, 2003; Van den Berghe and Levrau, 2004). These theories fall under the shareholder perspective as they advocate that the aim of corporate governance mechanisms, including the board of directors, is to increase shareholder value and protect owner interests (Letza et al., 2004). These studies therefore argues that board effectiveness depends on how well the boards perform their monitoring and strategic advisory roles (Adams et al., 2010; Forbes and Milliken, 248 N. Garcia-Torea et al. 1999; Kroll et al., 2008; Minichilli et al., 2012).

Corporate governance grading systems and Codes of Best Practices promote the formation of different committees to enhance board effectiveness (Van den Berghe and Levrau, 2004). Chen and Nowland, (2010) opine that firms with audit committees and remuneration committees are related to higher performance .Klein (1998) argues that board committees should be organized in two categories to contribute to board effectiveness: monitoring committees (audit, compensation and nomination committees) and Board of directors' effectiveness and the stakeholder perspective of corporate governance productivity committees (finance, investment and strategic committees).

Wen, Rwegasira & Bilderbeek (2002) analyzed the effects of Chinese listed firm's broad structure on the capital structure polices. The results suggests that higher board's corporate governance have impact on lower capital structure, on the other hand size of board member and capital structure revealed insignificant associations.

Nicholson and Kiel (2004) investigated the effects of corporate governance practices on capital structure decisions, dividend payout policy and firm performance of hundred peer firms' listed as non- financial companies in Pakistan for the period of 2006 to 2011. The results indicated that corporate governance mechanisms have positive significant relationship with financial decisions and firm performance indicators.

Mashayekhi and Bazaz (2008) examined the role of corporate governance indices on firm performance. They used data from companies listed in the Tehran Stock Exchange (TSE) for the years 2005–2006 .The results indicated a positive relationship between non-executive members on the board and financial performance of the companies listed in the Tehran Stock Exchange.

Ameer, Ramli and Zakaria (2010) investigated the link between board composition and firm performance using a board-level aggregation variable. They used linear regression to interpret panel data set of non-financial listed Malaysian firms over five years. The results showed that firm-boards with a high representation of outside and foreign directors are related with better performance compared to those firm-boards that have a majority of insider executive and affiliated non-executive directors. This confirmation supports the view of Zhang (2012) that the proportion of outside directors and CEO non- duality were negatively related with institutional and technical weakness ratings.

Hsu and Pongpitch (2010) investigated the link between corporate governance and efficiency performance of public non-life insurance companies in Thailand over the period of five years from 2000 to 2007.They used data envelopment analysis to compute the insurer‘s efficiency performance . The results indicated that there was an ambigous relationship between an insurer‘s efficiency performance and corporate governance attributes such as board size, proportion of financial expertise in audit committee and board compensation. This evidence contradicts the views of Mustafa and Youssef (2010) that an independent audit committee member is only effective if he or she is a financial expert.

Hsu (2010) examined the link between board features and financial performance of US firms with initial public offerings from 2000 to 2002. By using Tobin‘s Q, financial performance of the firms was measured and findings showed that board attributes (board expertise and educational background) positively related to firm performance. The evidence supports the analysis of Ujunwa (2012) whose findings indicate that the number of board members with Doctor of Philosophy (PhD) qualifications impacted positively on firm performance in Nigerian quoted firms. The return on assets or Tobin‘s Q is influenced by educational qualifications of board members and CEO especially (Darmadi, 2013).

Shan, George and Mclver (2011) analyzed the influence of corporate governance characteristics and corporate ownership on financial performance of Chinese companies from 2001 to 2005. They used used Tobin‘s Q to measure performance and found out that ownership concentration was significant in determining firm performance. The study emphasized that the expertise of the board was not a significant determinant of corporate financial performance in China.

Sami et al. (2011) explored the association between operating performance and corporate governance of Chinese listed companies. The studies indicated a favorable relationship between different measures of firm governance and performance.

Guo and Kumara (2012) examined the link between performance and corporate governance characteristics of listed companies on Colombo stock exchange in Srilanka. Their findings suggested a marginal negative association between board size and value of the firm, while a negative impact of proportion of outside directors on operating performance of company.

Nyamongo and Temesgen (2013) investigated the impact of corporate governance on the achievement of 37 commercial banks in Kenya over the period 2005-2009. They used two measures of performance, Return on Equity and Return on Assets, and regression analysis. The results indicated that the existence of independent board directors tends to enhance the performance of the banks in Kenya. This evidence justifies the views of Ameer, Ramli and Zakaria (2010) that firms with outside directors were associated with better performance. Moreover, the fraction of outside directors and CEO non-duality were negatively connected with institutional and technical weakness ratings (Zhang, 2012).

Webb (2004) studied the structure of boards of directors in 394 socially responsible firms and compared it to the structure of boards in a matched sample of non-socially responsible firms. She found socially responsible firms have boards with higher proportion of women and outsiders and less CEO duality than non-socially responsible firms. These features are some of the drivers of board effectiveness under the shareholder viewpoint. Being socially responsible is a way of responding to stakeholder interests; hence, we expect that firms with effective boards in protecting shareholder interests may be also more effective in promoting stakeholder interests.

Levrau and Van den Berghe (2007) argue that the success of the board of directors will also be determined by certain process variables such as cohesiveness, debate and conflict norms. They argue that much of the work that boards of directors do in order to produce effective results involves cooperative decision-making and joint efforts. A good degree of cohesiveness and working as a team is therefore essential for an effective board. A board as a decision- making group must be engaged in objective debates and with some conflict during the debates.

There is wealth of research work that has investigated the relationship of different Corporate Governance system and performance measures but the results, however, are not uniformly in agreement. This study is therefore focused on discerning the key determinants of effective boards of directors using data from publicly quoted companies in Namibia.

METHODOLOGY

A lot of studies on boards of directors have relied on quantitative data gathering techniques (Daily et. al.2003). These methods include mainly large archival data; while a subset of board studies have also used questionnaires. Levrau and Van den Berghe (2006), in their study of Belgium boards used a mixed method design (Teddlie and Tashakkori, 2003). They adopted a sequential exploratory design (Creswell et. al., 2003), which is a two phase approach in which collection and analysis of qualitative data in an initial phase is followed by a phase of quantitative data collection and analysis. Even though these methods offer the advantage to interpret the data in a consistent manner their access to process-oriented data is restricted (Daily et.al, 2003.

In this study the qualitative method was adopted to build on the strength of previous research. In the first phase of the research, we selected purposively utilizing a critical cases sampling scheme (Collins et.al, 2006). This meant intentionally limiting the sample to members of the boards of directors of Namibian listed companies because we believed that they are well-placed to provide us with compelling insights into the determinants of board effectiveness.

A sample of 122 directors of Namibia companies listed on Namibian Stock Exchange were contacted and asked to participate in a large scale in-depth study on corporate governance in Namibia. The sample included different directors' roles such as CEOs, chairmen, independent directors and non-executive directors. Data on the companies listed on Namibian Stock Exchange was found on the Namibian Stock Exchange website (www. nsx.com.na). Information on the boards of directors was recovered from multiple sources such as the company's annual report, and their websites. Of the initial 122 directors that were contacted, a total of 87 (response rate = 71 %) agreed to participate. Table 1 presents our sample in terms of directors' roles.

Table 1: (Qualitative) sample per directors' role

Chairmen	**29**
Chairman= CEO	3
Chairman =Independent director	10
Chairman = non-executive director	16
Executive directors	**27**
CEOs	20
Other executives	7
Non-executives directors	**31**
Independent directors	23
Non-executive shareholders' representatives	8
Total	**87**

Data was collected during interviews with directors of Namibian listed companies. For the purpose of this study, a standardized open-ended question was used (Johnson and Turner, 2003). The directors were asked to sum up what they understood as the most important elements of a good board of directors. The word 'effective' was deliberately not used to avoid misunderstanding because the concept of effectiveness may give different interpretations. The word 'good' was used by consequence. The questions were phrased in a more impartial way for each respondent to have same understanding of the question, which diminishes bias in the answers. Open-ended questions were used in order to fully capture a broad spectrum of criteria.

RESULTS

The interviews yielded a vast set of feedback regarding criteria that signify a good corporate board, as understood by the directors. Table 2 provides a summary of the results.

Table 2: Elements of a good corporate board - directors' perspectives

Families	No. of respondents who referred to this criteria	% of respondents (N=87**)**	Frequency this criteria was reported
Criteria 1: board structure	80	92%	**N=84**
Criteria 2: board ethos	44	50%	**N=46**
Criteria 3 : board operation	41	47%	**N=45**
Criteria 4: board duties	27	31%	**N=30**
Criteria 5: discussion/decision-making	24	27%	**N=25**
Criteria 6: individual norms	21	24%	**N=24**
Criteria 7: relationship between the board members	19	22%	**N=20**
Criteria 8: board-management relationship	5	6%	**N=5**

The results presented in table 2 above illustrate that issues related to the structure of the board are frequently reported by a great number of directors. Board ethos which depicts unquantifiable aspects of the board of directors occupies the second place followed immediately by the board operations. The other criteria are considered to a lesser extent .The criteria are discussed below:

Board Structure: In directors' views, in order to be effective, the board of directors needs to have the appropriate structure which involves features like diversity. This entailed a thoughtful nominations and a non-political affiliation recruitment process that is viewed as parts of a broader effort to identify, involve, and develop board leadership that is a mix of people having different personalities, educational and occupational backgrounds.
Board Ethos. Most directors raised the aspects of openness and transparency and ability to express their views and a culture of open debate. This implied that affairs of the companies should be treated inside the boardroom and not 'behind the scene'.
Board operations. The directors highlighted the significance of being thoroughly prepared and that sufficient information must be provided for each point on the agenda in such a manner that it allows directors to decide with full knowledge during board meetings
Board duties. A number of directors affirmed that, a good board of directors should have some insight into the evolution of the business environment in order to effectively execute their duties
Discussion/decision-making. Emphasis was made to have real, in-depth discussion characterized by neutrality and objectivity and decision ought to be made by board members.
Individual norms. Aspects such as integrity, ethics, attitude, and ego were mentioned as well as emphasis on the commitment of individual directors referring to the personal enthusiasm, interest and availability of people sitting on a board.
Relationship between the board members. The directors highlighted the need for the board of directors to function as a team. Finally, trust and respect between the members be cherished.
Board-management relationship. More specifically, this aspect relates to the contact with and trust in management, as well as to the quality of management. Only a few directors mentioned the reliance of the board on a strong and honest management as a key criterion for its effectiveness.

DISCUSSION

Even though boards of directors are regularly studied in academic research, intellectuals have traditionally focused on a limited number of characteristics such as board size, board composition and board leadership. These structural measures are generally viewed as appropriate and adequate alternates for understanding board effectiveness, while the working processes of boards or individual directors' behaviour are rarely explored. A number of research streams advance that if the structure of a board is appropriate, the board should be able to accomplish its duties, and eventually enhance corporate performance. Be that as it may, little convincing evidence exists that these structural measures, which are assumed to contribute to the effectiveness of boards as preserver of shareholders' welfare, have had substantial impact on the financial performance of companies.

The results suggest that board of directors and board effectiveness in particular, should also be understood through attributes reflecting the board's inner workings and not solely through attributes of board structure and composition. The results of the studies also indicate the significance of having a sufficient mix of directors' roles in terms of executives, non-executives and independent directors, they suggest that competencies, diversity and complementarity are more pivotal attributes for board effectiveness. These criteria were among the most cited in the interviews and the dimension of complementarity systematically received high rankings in the questionnaires.

Mutual relationships between the board members also was also highlighted .Even though the frequencies are quite low, some related factors could be singled out. The boards need to foster cohesiveness, a stimulated interaction among the directors and value towards trust and respect between the members.

The study also points out that those boards whose directors have a greater amount of relevant information appear to perform their roles more effectively than boards that are less well informed.

CONCLUSION

Many empirical studies have presumed that the effectiveness of the board is a function of its structure and independence from management. A couple of studies have undertaken to adopt an all-inclusive approach by reviewing the outcome of board processes, functions and behaviour on the effectiveness of the board. This study proves that process variables and, to a lesser extent, demographic variables greatly impact board duties performance. Boards fulfill their duties well through cooperation, discussion and quality decision making based on quality information.

This study clearly shows that many aspects of board effectiveness are invisible to 'outsiders' and as a result poorly understood. Many researchers have stayed at a considerable distance from actual board practice, somewhat because of difficulties of gaining access. Notably, they focus their attention on a small number of structural board characteristics leading to inconclusive findings.

Generally, in order for boards to function well it is not sufficient to demand changes in board demography however boards must devote more attention to their in-house processes.

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