Influence of Professional Expertise on Dividend Policy among Listed Firms in Nairobi Securities Exchange in Kenya

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Abstract

Management of corporations has been faced by challenges emerging from internal managers not being able to effectively offer stewardship. The organizations owners therefore have to improvise means of ensuring that their interests are protected. In modern corporation's owners embrace mechanisms like board diversity to mitigate against managers failures to act in their interests. The purpose of this study was to examine the influence o professional expertise on Dividend Policy among listed firms in Nairobi Securities Exchange. In the recent past, most corporations in developing economies experience unstable dividend payment hence the need to determine whether professional expertise can remedy dividend payment situation prevailing. The study examined how professional expertise can influence dividend policy in companies listed on the NSE. The study was guided by agency, signaling, resource dependency and power circulation theories. The study used the explanatory research design. Document analysis was used to collect secondary data from annual reports of firms. Data was analyzed using descriptive statistics such as the mean, median, and standard deviation and fixed effect multiple regression analysis was done to examine the effects between professional expertise and dividend policy in annual reports of firms. The study was also expected to contribute new knowledge on the relationship between professional expertise and dividend policy. The regression results showed that professional expertise (β = .226, p = .490) exhibit a strong direct relationship with dividend policy. The study recommends that policy makers to ensure development of regulations to enhance professional expertise among firms since professional expertise brings about overwhelming benefits to corporate owners by minimizing agency problems related to free cash flows hence enhance payout to shareholder and reduce risk of misallocation of excess resources by firm managers. The study also recommends further studies to be carried out on the relationship between professional expertise and dividend policy on privately owned, SME's, both listed and unlisted firms using similar study variables and a longer period for the same study to determine whether optimal results would be achieved.

Keywords: Professional Expertise, Dividend, Policy, Resource dependency, securities exchange

INTRODUCTION

Research on professional expertise of corporate directors has generally focused on the existence of a specific type of professional expertise legal, banking, accounting, political or outside CEOs (Agrawal &Knoeber,2001; Fich, 2005, Guner*et al*., 2008). Andeson*et al*., (2011) examined multiple types of expertise. Their measures of professional expertise include the existence of consultants, accountants, lawyers, bankers and outside CEOs on the board. Jensen, (1993) and Khein (1998) argue that boards comprising directors from different business and socioeconomic backgrounds bring different perspectives to their monitoring and advisory roles that would provide benefits to business owners thorough improved problems solving, strategy formulation and resource utilization. However, Putnam, (2007) and Baranchuk and Dybrig, (2009) postulate that directors from diverse backgrounds can create conflicts in the boardroom hence slow down decision making, impends communication and leads to social loafing. Some study indicates that diversity result to increased cost of communication and higher team member turnover (Arrow,1986, and Lang, 1986) hence; it is not clear whether less or more professional expertise diversity on the board is in the best interest of the shareholders.

Professional expertise of directors have been examined by researchers generally focusing on the existence of a specific type of professional expertise. Defond*et al.*, (2005) examined directors with financial expertise and found that the market reaction to new director appointment is higher if the director has financial expertise which is relevant to the company's audit committee. Fich (2005) examined directors with CEO experience and indicated that announcement of returns is higher for directors with expertise of a CEO of another listed company. Francis *et al*., (2013) examined directors with different types of academic expertise. The study overly provides supportive evidence that academic directors are valuable advisors and effective monitors hence firms benefit from having academic directors.

Gray and Nowland (2014) carried a study on professional expertise and board diversity hence indicates that most common types of professional expertise on corporate boards are accountants, lawyers, bankers, business

executives, engineers and scientists. They also found that some types of professional expertise are clustered in certain industries like scientists (materials, energy and health care), banker (financial), engineers (materials, energy and industrials) and academics and doctors (healthcare) while other types of expertise are prevalent across all industries (accountant, executive, lawyers, and bankers). The researcher did not find any relationship between professional expertise diversity and firm's value. Gray and Nowland (2004) find evidence that shareholders benefit when firms limit their board diversity to a specific subset of professional expertise (lawyers, accountants, consultants, bankers and other CEOs).

Based on the resource dependence theory this study seeks to determine whether professional expertise has a great influence on dividend policy in Kenyan firms.

MATERIALS AND METHODS

Research Design

John *et al*. (2007) defined research design as a blueprint for fulfilling research objectives and answering research questions. It is a master plan specifying the methods and procedures for collecting and analyzing the needed information. This study adopted an explanatory research design. Explanatory study examines the causal relationship between variables with an aim to explain the relationship between the independent and dependent variables (Thornhill *et al.,* 2000 and Orodho, 2003). The explanatory research design was deemed appropriate since it enables the study to be carried out in a natural setting. The study was longitudinal survey in nature since data was collected for a period of 7 (seven) years from 2007 to 2013.

The Study Area

The Study was conducted in firms listed on the Nairobi Securities Exchange for the period ranging from 2007 to 2013. Allfirms listed at the NSE were targeted. The firms were categorized into; Agricultural, Automobile & Accessories, Commercial & Services, Construction & Allied, Energy & Petroleum, Insurance, Investments, Investment Services, Manufacturing & Allied, Telecommunication & Technology and Growth & Enterprise Market Segment. Firms listed on the NSE were targeted because it was easy to access their annual reports through the Capital Market Authority library for the purposes of data collection and analysis since they were actively traded and are also audited by independent auditors hence makes data more reliable.

Target Population

The study targeted all firms listed on the Nairobi Securities Exchange (NSE). Currently NSE has64 listed firms. The study examined the entire population of sixty four (64) firms from all the sectors as categorized by the Nairobi Securities Exchange among the investment segments. The number of firms in Agricultural, Automobile & Accessories, Banking, Commercial & Services, Construction & Allied, Energy &Petroleum, Insurance, Investments, Investment Services, Manufacturing & Allied, Telecommunication & Technology and Growth & Enterprise Market Segment.

Sampling Design and Procedure

The study employed census to select population of the study among the listed firms on the Nairobi Securities Exchange. The census refers to a survey that collects data from all members of a population, whether it's people or businesses (Sekaran, 2003). The census was employed since the population was small and to ensure that all members of the population has a chance to be studied. Due to the relatively small number of firms listed on the Nairobi Securities Exchange (64), all firms were considered for inclusion in the survey.

Purposive sampling was employed in order to achieve consistency in the study (Mugenda and Mugenda, 1999). At least 70% of firms in each of the sectors were represented in the survey.

Data Collection Method and Instruments

Content analysis technique was used to obtain data from annual reports of firms listed on the NSE between 2007 and 2013.Data from annual reports on both the independent and dependent variables as indicated on the conceptual framework was collected from all the firms chosen for the study. Document analysis guide was used to collect data on the indicators of age diversity and dividend policy. This was for the period of study ranging from 2007 to 2013. According to Oso and Onen (2005), document analysis is an instrument for collecting unobtrusive information. Document analysis was used since data to be collected are of secondary nature, which would enabled the researcher to collect data without interruption and it would save time.

Prior studies on board age diversity have measured age in terms of dispersion of age of all board members. Siciliano (1996) measured this variable by dividing ages of board members into five categories; under 20, 20-35, 36-50, and 51-65 and over 65. The data collected provided information in total percentages in each age category. The diversity scale was calculated as a percentage in each age category, the highest percentage of any sub-groupings is subtracted from 100 (a higher score representing greater diversity) hence multiplied by the total number of categories with any amount of representation (Siciliano, 1996). Other scholars have used the average age of the board for robustness check of results (Waelchli & Zeller, 2012; Carter et al., 2010; Marinova *et al.*, 2010). McIntyre *et al*., (2007) measured board age diversity as a standard deviation of ages. In this study age diversity was measured in terms of the method used by Siciliano (1996) where dispersion of ages was considered

and also the method adopted by Mclntyre *et al*., (2007) where standard deviation of ages was utilized.

Data Collection Procedures

The researcher carried out pre-test of the research instruments to ensure reliability. A sample of firms listed on the NSE was selected for this activity and any corrective measures executed in order to enable the instruments reliability for data collection. The research assistants were identified and briefed on the research process including data collection instruments while taking into consideration the ethical issues that may be likely to arise in the course of the data collection.

Data Analysis

The data was gathered from annual reports of the firms listed on the Nairobi Securities Exchange. The information elicited was presented quantitatively. The EViews 7 Statistical package was used to perform all the analysis for the study. Descriptive statistics was performed for the independent and dependent variables of the study which are dividend policy, professional expertise. This statistics are mean, median, and standard deviation. A correlation was also carried out between the study variables which are dividend policy and professional expertise. Regression analysis was also carried out to determine the effect of professional expertise on dividend policy. Fixed effect multiple regression analysis was performed using the following model:

$Y_{ij} = a_0 + X_{2ij} + \varepsilon$

Where Y_{ij} =   Dividend policy

X_{2ij} =   Professional expertise

a_0 =   A constant or the value of Y when all X values are Zero.

ε =   The error term, normally distributed about a mean of 0.

Reliability of the Instruments

Reliability reflects the consistency that instruments demonstrate when applied repeatedly under similar conditions (Kerlinger 1983). Before actual data analysis the researcher will establish reliability of the research instruments. This was done using internal consistency technique. A sample of firms that qualify for the study from the study sample was taken for the test hence correlated among the study items for a similar period of research.

Validity of the Instruments

Concurrent validity of an instrument is demonstrated when an instrument is seen to predict the behaviour of subjects in the present and not in the future (Mugenda and Mugenda, 1999). To test validity of the instruments used in this study, a pilot study was conducted on firms listed on the Nairobi Securities Exchange for the period 2007 to 2013. This will give the position on past and future behaviour on dividend policy of firms listed on the NSE. Construct validity was attained since the study was for a period of seven years for all the sampled firms listed on the NSE. On the other hand, content validity was achieved by the identification of the indicators of gender, age, ethnicity and professional expertise as well as the indicators of dividend policy. This ensured that all the relevant information is captured to enhance validity.

ANALYSIS, PRESENTATIONS AND INTERPRETATIONS

Table 4.1. Descriptive Statistics

Variables	Dividend Policy	Professional Expertise
Mean	1.211	0.510
Median	1.264	0.500
Maximum	3.296	0.920
Minimum	-0.799	0.170
Standard Deviation	0.666	0.198
Skewness	-0.447	0.203
Critical ratio Skewness	-3.362	1.533
Kurtosis	3.496	2.040
Critical ratio Kurtosis	13.218	29.161
Observations	343	343

Source (Data survey, 2018)

The dividend policy had the highest and lowest values of 3.296 and -0.799 respectively resulting to a range of 4.095. On an average a firm paid dividend of 1.2 per share. The standard deviation indicated a variation of .67, the results hence shows that there was a high variation in dividend payout among the listed firms on the NSE. Professional expertise had the highest and lowest scores of .92 and .17 respectively resulting to a range of .75 with a mean of .51 and a standard deviation of .20 which postulate that there was a low variation in professional expertise among companies listed on the NSE.

Correlation Results

Pearson correlation analysis was carried out to determine the correlation among study variables. The Pearson

correlation between professional expertise and dividend policy was negative (r = -.097, p = .073) and significant. This implies that professional expertise was an important factor in influencing dividend policy. The Pearson correlation between professional expertise and corporate size was positive (r = .399, p = .000) significant. These indicate that the variables have .4 common variability. The Pearson correlation between professional expertise and foreign diversity (r = -.170, p = .002) and age (r = -.125, p = .02) were negatively correlated and significant. These implies that the association between professional expertise and foreign diversity and age had negative common variability of -.17 and -.13 respectively. The Pearson correlation between professional expertise and leverage was positive (r = .035, p = .514) but insignificant. These implies that there are high chances of improvement in the association between the variables. The Pearson correlation between professional expertise and gender (r = .086, p = .112) was positive but insignificant.

Normality Test

According to Gujarrati and Porter (2009) normality test must be exhibited before a study can proceed on with other regression tests like autocorrelation, multicollinearity and heteroscedasticity. Normality test confirms whether the error terms are normality distributed or not in the model. In this study the critical ratios of skewness and kurtosis highlighted in Table 4.1 on descriptive statistics was used to the normality assumption of the error terms on the regression model. The study found that on all the variables the skewness and kurtosis values were below the critical values of skewness and kurtosis respectively, therefore indicated that the data for the study was normally distributed (Hair *et al*., 2006). The study also in Table 4.1 employed the Jarque-Bera statistics to test normality of the data whose results indicated existence of normality of the distribution since the Jarque-Bera Statistics for both the dependent and independent variables were large and significant. The central limit theorem also states that when a study sample size is more than 100 observations the data tends to be normally distributed (Gujarrati and Porter, 2009).This study had 343 firm year observation which indicates that the central limit theorem on normality of distribution was fulfilled hence this model is normally distributed.

Hypothesis testing

There is no Significant Relationship between Professional Expertise and Dividend Policy

The regression results on the relationship between professional expertise and dividend policy are reported on Table 4.7. The results indicate that there was no any significant relationship in all the three models (2, 3 and 4). The beta's were positive (β = .226, p = .490;β = .263, p =.425; andβ = .544, p = .314) for models (2, 3, and 4) respectively. Therefore, in all the affected models the null hypothesis were accepted that states Ho_2.There is no Significant Relationship between Professional Expertise and Dividend Policy. The t values for the three models (2, 3 and 4) were positive (.798, 1.118 and 1.009) respectively which implies that there was minimal association between professional expertise and dividend policy. The results supported the hypothesis of the study which was inconsistent with a prior study by Hsu (2010) on the relationship between board characteristics and financial performance where the results posted a positive outcome on board quality measured by board expertise and educational background. Tornyera and Wereko (2012) also in their study found a positive association between board skills and management skills and firm performance. Thomas and Gregory (2014) in their prior study postulate that a professional board consisting of retired executives with industry-specific expertise is vulnerable to groupthink mentality, as well as to the availability of such individual board directorship seats. The study further indicates that while industry-specific expertise's is a desired attribute of an independent board director, there are other attributes that firms look for, such as international, regulatory/government, risk, technology, and marketing expertise. In a study by Craig and James (2009) they found that firms having academic directors on their board have greater board demographic diversity than firms without academic director hence firms with academic directors have the same average emphasis on knowledge-based earnings as other firms. Powell (1991) postulate that there may be a negative relationship between skill levels and firm performance due to the occupational and professional affiliations of highly qualified managers which increase agency behavior.

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

Summary of the findings

The hypothesis that there is no significant relationship between professional expertise and dividend policy in Kenya. Professional expertise was defined as the ratio of financial expertise in the board divided by the total number of directors on the firm board. Professional expertise was diversified with a mean of .51 with a range of between minimum of .17 and maximum of .92. The study postulates that there was no significant relationship between professional expertise and dividend policy in Kenya. The study outcome does not support prior findings by Craig and James (2009), Hsu (2010), Tornyera and Wereko (2012), and Thomas and Gregory (2014) which posted positive relationship between professional expertise and dividend policy.

Conclusion

The study was grounded on agency, signaling, stakeholder and power circulation theories. According to the study findings, it was found that gender diversity was the most important variable in determining the relationship between board diversity and dividend policy decisions in Kenya. Professional expertise exhibited minimal

association with dividend policy. These could be as a result of company's failure to include in their boards persons with financial expertise.

Recommendations for Practice and Policy

In view of the findings and conclusions of the study found out that professional expertise had minimal association with dividend policy which was contrary to practice as alluded to by other authors like Hsu (2010), Tornyera and Wereko (2012) and Thomas and Gregory (2014). The study therefore, recommends that Capital Market Authority and Nairobi Securities Exchange comes up with regulations to fully enforce the Capital Market Authority Act which has a provision on appointment of board members with diverse professional expertise to enhance compliance with the law. The shareholders stand to benefit from diverse professional expertise due to contributions that would add value to the posterity of the firm hence high returns to the company owners.

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