

The impact of board composition on shareholder wealth creation: evidence from public companies in Sri Lanka

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ABSTRACT

Purpose — *This research aims to examine the impact of board composition on shareholder wealth in line with the agency and resource dependency theory approach due to the poor corporate governance practices leading to investors' lack of confidence.*

Method — *The study samples included companies listed on the Colombo Stock Exchange in Sri Lanka. The banks and financial institutions were excluded from this study. The study period consists of seven years, and a final sample of 175 companies was selected for the analysis. E-View 9 statistical software was used to test the association between Board composition-related variables and shareholder wealth.*

Result — *The findings revealed that board size, separate leadership structure, and proportion of non-executive directors on the Board positively influence shareholder wealth. At the same time, a separate leadership structure also tends to enhance the shareholder wealth of companies. It is noted that a large board and a higher proportion of non-executive directors on the Board would benefit shareholders, which supports the theoretical prediction of agency and resource dependency theories and the code of best practices on corporate governance in Sri Lanka. The result related to women's representation on the Board does not significantly influence shareholder wealth since the gender balance was not prioritized in Sri Lankan listed companies.*

Recommendation — *The findings provide valuable information to professionals and policymakers to develop a framework for corporate governance systems. It is also advisable to consider the gender balance on board affairs. Corporate governance mechanisms are considered important factors in protecting shareholder interests at large.*

Contribution — *There were few studies in Sri Lanka that specifically examined corporate governance best practices and their impact on firm performance, but no single study directly addresses the shareholder wealth of listed companies in Sri Lanka. This study is intended to fill in this gap.*

Keywords: *corporate governance, shareholder wealth, board composition, Colombo Stock Exchange, agency theory, resource dependence theory*



INTRODUCTION

The concept of corporate governance has been considered globally after corporate failures like Enron and WorldCom ([Mustapha and Ahmad, 2011](#)). Such failures and corporate scandals have raised serious concern among professionals and academics on the effectiveness of corporate governance in the corporate world. It has also become a debatable topic in Sri Lanka due to corporate failures such as Pramuka Bank, Seylan Bank, Golden and Key Finance Company. This raises a major concern about the implementation of effective corporate governance practices among the companies listed in Sri Lanka as well as in the global context. In the meantime, Sri Lanka-based companies continuously recorded higher performance and gradually increased their firm value ([Kalainathan and Vijayarani, 2014](#)). However, despite having such remarkable achievements in the past, the current corporate governance practices, as studies revealed, are not aligned with the standard, and there is variation between the standard practices and existing practices of corporate governance in Sri Lankan companies ([Dissabandara, 2012](#)).

The conflict-of-interest index reveals that investors are unhappy with their investments in Sri Lanka. Therefore, they focus more on their return on investment and the effectiveness of corporate governance practices in Sri Lanka. Due to the ownership concentration, the implementation of independent directors' system is much more challenging in Sri Lankan companies ([Senaratne and Gunaratne, 2008](#)). [Weerasinghe and Ajwad \(2017\)](#) identified existing issues of corporate governance practices in Sri Lankan companies: corporate governance regulation and compliances are not prepared in consultation with stakeholders, and there is weakness in the assessment of the Board of directors periodically and weakness of regulatory framework. [Gunathilake, Chandrakumara, and Zoysa \(2011\)](#) pointed out that the reason for the weakness of the regulatory framework is that political interferences often affect the implementation of the regulation in the country. It also raises serious concern on to what extent the existing corporate governance mechanisms (board composition) influence maximizing shareholder wealth of companies listed in Sri Lanka in the context of the agency and resource dependency theory approach.

Corporate governance aims to set up effective controlling systems to ensure the corporate objectives are achieved, such as maximizing profit and shareholder wealth ([Kiel and Nicholson, 2003](#)). Corporate governance best practices were set up and implemented periodically to have effective controlling systems in the organization to attract investors and enhance the growth of companies as well as the economic growth of the country. Corporate governance standard is much more important to align the interest of managers and shareholders, which

resolves the conflict of interest. It also allowed the corporations to cut agency costs associated with ownership and control separation ([Dissabandara, 2012](#)).

The corporate governance reforms process was carried out in Sri Lanka in the late 1990s. After that, in 1997, companies registered on the Colombo Stock Exchange in Sri Lanka accepted a voluntary code of corporate governance best practices to protect their shareholders' interests. A few years later, all companies listed on Colombo Stock Exchange followed a mandatory and voluntary code of best corporate governance practices. Then, they were adapted to mandatory compliance with corporate governance practice Rome 1st April 2008 ([Senaratne and Gunaratne, 2008](#)).

Corporate governance practices in industrialized countries are distinct from those in underdeveloped nations. It is also suggested that corporate governance methods of Norwegian and Russian enterprises vary based on the political, economic, social, and technological backdrop ([Garanina and Kaikova, 2016](#)). [Dharmadasa, Gamage, and Herath \(2014\)](#) state that corporate governance practices of companies in Sri Lanka also vary among the firms and industry. It is also pointed out that the research findings from the developed country will not apply to the developing market. Many corporate governance-related types of research were carried out in U.S and western countries' contexts ([Kiel and Nicholson, 2003](#)). Little research focuses on shareholder wealth ([Azhagaiah and Priya, 2008](#); [Boatright, 2010](#); [Prempeh and Odartei-Mills, 2015](#)).

There have been few studies contextualized in Sri Lanka that examine corporate governance best practices and their impact on firm performance ([Azeez, 2015](#)), but no single study directly addresses the shareholder wealth in listed companies in Sri Lanka. The originality of this study is the inclusion of the knowledge concerning shareholder wealth maximization as proposed by the theories related to agency theory and resource dependency theory. This study also highlights the impact of gender diversity on shareholder wealth maximization, which adds more value to this research work in the Sri Lankan context.

The purpose of this study is to examine the impact of board composition, including board size, separate leadership structure, the proportion of non-executive directors on the Board, and the representation of women in the shareholder wealth creation of companies listed in Sri Lanka within the context of agency and resource dependency theory.

LITERATURE REVIEW

Agency theory

The concept of corporate governance leading to maximizing shareholder wealth is backed by many theories like agency theory, resource dependence theory, and shareholder theory (Means, 2017; Hillman and Dalziel, 2003; Smallman, 2004; Tse, 2011). Agency theory proposes the most effective corporate governance approaches to handle the inherent conflict of interest between managers and shareholders. It states that the Board of directors is responsible for protecting the interest of shareholders through maximizing shareholder wealth. It is pointed out that managers involve in wrong decision making which does not increase the wealth of the firm. Jensen and Meckling (1976) stated that it is thus important for the directors to observe the management action to mitigate the misappropriation of assets. Agency theory also proposes effective corporate governance mechanisms which will enhance the shareholder wealth of the firm. It is also proposed that the representation of non-executive directors on the Board should be more than the executive directors to monitor management actions (Fama and Jensen, 1983). Kiel and Nicholson (2003) stated that there should be a separate leadership structure for the firm in which the Chairman of the Board must be independent of the Chief Executive Officer of companies to overcome bias in decision making. Agency theory predicts that if one person holds a dual role, then the interest of the shareholders will not be achieved.

Resource dependency theory

Resource dependence theory proposes corporate governance mechanisms similar to agency theory. It highlights that the Board of directors must exchange internal and external resources to achieve the objectives of the organization (Hillman and Dalziel, 2003). It suggests that non-executive directors are represented from outside the organization and inform decision-making. Resource dependence theory also proposes that board diversity is the main concern of corporate governance mechanisms. It holds an argument that the Board of directors must consider the gender differences in set-up the Board (Hillman, Cannella, and Harris, 2002).

Hypothesis

Board size

In Sri Lanka, listed companies must be governed by an effective board of directors who follow the code of best corporate governance practices. The

success or failure of the companies depends on the effective governance system. There were many arguments on board size and whether the company must have a smaller or larger board to govern the firm to reach its objectives. [Florackis \(2008\)](#) states that board size determines board effectiveness. [Singh and Davidson \(2003\)](#) further suggest concern on board size since it highly leads to board effectiveness to formulate strategies and monitor management action to protect the expectation of shareholders. Still, there is an ongoing argument among the researchers on whether small or large boards are effective in the corporate governance system, but research findings are inconclusive or inconsistent in this regard.

As far as theories are concerned, the agency theory recommends that the Board of directors should have a large number of directors to oversee resource utilization effectively. Resource dependence theory also argues similarly to agency theory that a larger number of boards of directors will have greater access to resources inside and outside firms which will then enhance the performance of the firm ([Kiel and Nicholson, 2003](#)). [Reddy and Locke \(2014\)](#) stated that to balance the right talents and knowledge of directors, a larger board is preferable to a smaller board. On the other side of the argument, [Florackis \(2008\)](#) suggest having a smaller board that will be easy to coordinate, communicate, and make a decision. There are few studies focused on shareholder wealth maximization. [Tchouassi and Nosseyamba \(2011\)](#) conducted research from an African perspective and state that increasing the board size leads to maximizing shareholder wealth which is proof of all variables tested in the study. [Prempeh and Odartei-Mills \(2015\)](#) point out that board size does not significantly influence shareholder wealth measured with dividend yield but positively influences shareholder wealth measured with dividend per share as a proxy to shareholder wealth. Therefore, as suggested by the theories, the hypothesis of the study is:

H₁: Board size influences shareholder wealth

Separate leadership structure

The code of best practices on corporate governance emphasizes the need for listed firms in Sri Lanka to have strong leadership to address the conflict between management and shareholders. It further suggests separating the position of Chief Executive Officer (CEO) and Chairman of Board (COB) to balance the power and authority, which will enhance the power of decision making. Separating the roles of COB and CEO can improve board effectiveness while also reducing agency conflict ([Florackis, 2008](#); [Gul et al., 2012](#)). Similar to

the code of best practices for corporate governance, agency theory recommends segregating the position.

Kiel and Nicholson (2003) researched CEO duality and firm performance. They concluded that the majority of firms in their study would practice separating the position of COB and CEO, which lead to better board performance. They further suggest that CEO duality results in poor performance of firms. Gul et al. (2012) found a negative relationship between CEO duality and assets utilization ratios which result in influencing the decision-making of the Board and then lead to higher agency costs which will destroy shareholder wealth maximization. Prempeh and Odartei-Mills (2015) state that the results on the leadership structure of a listed firm and shareholder wealth maximization are inconclusive. Therefore, as suggested by agency theory, the hypothesis of the study is:

H₂: Separate leadership structure influences shareholder wealth

The proportion of non-executive directors on the Board

Agency theory highlights the importance of including non-executive directors on the Board, which will bring information and resources to companies in creating sustainable advantage (McKnight and Weir, 2009). The presence of a majority of non-executive directors on the Board would result in robust governance structures for monitoring management actions and making sound decisions (Garanina and Kaikova, 2016; Florackis, 2008). Kiel and Nicholson (2003) state that a higher proportion of non-executive directors on the Board influences the enhancement of the performance of the firm. The board performance highly depends on board composition, including non-executive directors on the Board who will direct to maximize shareholder wealth.

There is an argument against the representation of non-executive directors on the Board. Florackis (2008) stated that non-executive directors lack knowledge of a company's operations and lack the necessary skills to lead it. The study reveals that the representation of non-executive directors on the Board does not have any significant impact on firm value in the U.K. This implies that the independent director system does not ensure the adoption of objectives of the corporate governance system in maximizing shareholder wealth (Prempeh and Odartei-Mills, 2015). Since the results related to corporate governance practices and their influence on shareholder wealth maximization are inconclusive (Reddy and Locke, 2014), as suggested by agency theory, the hypothesis of the study is:

H₃: Proportion of non-executive directors on boards influences shareholder wealth

Representation of women on the Board

Women's representation in companies' affairs has been a debatable topic globally. There is an ongoing argument on their contribution and impact on the company's performance. Many corporations are undertaking women's representation in their companies' operations to enhance their performance. A study on women's participation in board performance shows that female directors have a direct and positive impact on companies' performance (Guy, Niethammer, and Moline, 2011). It has been proved that shareholder wealth can be maximized through board diversity (Carter et al., 2003). Gender diversity contributes to organizational success in many ways, such as enhancing innovation, leading to effective problem solving and leadership, and moving the company to a global level which enhances shareholder wealth. There are nations with quota systems for women's participation in company activities, although the percentage of female board members in Australia, France, Europe, Sweden, and Norway is 8.3%, 7.6%, 9.7%, 26.9%, and 44.2%, respectively. Tudawe (2010) remarks that participation of women in Sri Lankan companies is only 1% or less than one per cent.

Agency theory and resource dependence theory promote board diversity among the firms, which would enhance firm value. Empirical pieces of evidence related to board diversity and firm performance leading to shareholder wealth are inconclusive. Research findings reveal that there is no consistency or mixed results in the relationship between board diversity and firm value (Carter et al., 2010). Contrary to popular opinion, few research studies support the thesis of agency theory that there is a positive correlation between the proportion of women on the Board and the value of the company (Adams and Ferreira, 2009; Carter et al., 2003; Guy et al., 2011). It is noted that board diversity tends to allocate more resources and monitoring mechanisms of management actions and decision making. As suggested by the theory, the hypothesis of the study is:

H₄: The proportion of women on board influences shareholder wealth

Conceptual framework

Agency theory proposes a way to create shareholder wealth through introducing corporate governance best practices in an organization. Shareholder wealth maximization primarily depends on the Board of directors (Kiel and Nicholson, 2003). The Board of directors plays an important role in directing the organization to achieve its objectives. Agency theory proposes that having a higher proportion of independent directors on the Board is effective (Fama and Jensen, 1983). Independent directors play a crucial role in providing information

to the company and scrutinizing the executive directors' decisions. Agency theory also addresses the importance of separating the position of CEO and COB, which will protect the interest of shareholders (Kiel and Nicholson, 2003). The conceptual model of this study and development of the hypothesis is based on agency theory, resource dependency theory and previous works of literature. The conceptual framework below highlights the connection between corporate governance variables such as board size, separate leadership structure, the proportion of independent directors and women on the Board, and shareholder wealth.

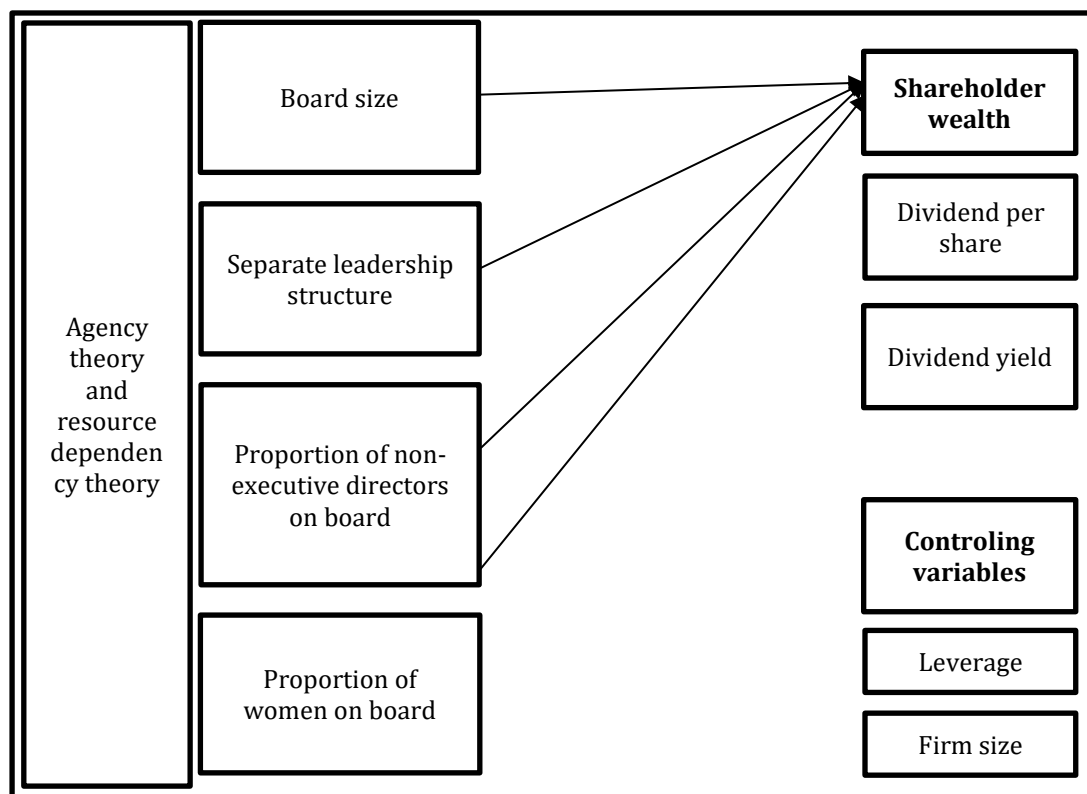


Figure 1. Conceptual framework
 Source: the author (2022)

RESEARCH METHOD

Variable measurement

In order to analyze the influence of corporate governance mechanisms on shareholder wealth maximization in this study, board size is measured as the total number of directors on the Board (Florackis, 2008; Garanina and Kaikova, 2016; Gul et al., 2012; Kiel and Nicholson, 2003; Prempeh and Odartei-Mills, 2015; Reddy and Locke, 2014). This study uses dummy variables for board

leadership structure. If combined with leadership, the position is coded '0'. If separated, it is coded '1'. In this study, non-executive and independent directors on the Board are determined by dividing the number of non-executive directors by the total number of directors (Donaldson and Davis, 1991; Florackis, 2008; Gul et al., 2012; McKnight and Weir, 2009; Reddy and Locke, 2014). Women on Board are measured as the proportion of women's participation to the total number of board directors (Carter et al., 2010; Guy et al., 2011). Shareholder wealth is measured in terms of dividend yield and dividend per share. The dividend yield is calculated by dividing the total dividends paid to shareholders by the market price of the shares. Dividend per share is the ratio of total dividends paid to the number of outstanding shares (Chilosi and Damiani, 2007; Kyereboah-Coleman, 2007; Prempeh and Odartei-Mills, 2015; Tchouassi and Nosseyamba, 2011).

Population and samples

The samples used in the study consisted of all public companies listed on the Colombo Stock Exchange. Financial institutions and banks are removed from the samples due to their unique ownership and management structure. The period of the study consists of seven years, from 2013 to 2019. The final samples consisted of 175 listed companies. Corporate governance practices were revised in 2003, 2007, and then 2013. During this period, many scholars have critiqued the corporate governance practices of Sri Lankan listed companies. Therefore, it was important to examine the effectiveness of the board structure in maximizing shareholder wealth after this period.

Method of analysis and estimation model

E-Views 9 statistical software was used to test the relationship between structure-related variables and shareholder wealth during the aforementioned period by using secondary data. The analysis includes descriptive statistics, Spearman's correlation, multiple regression analysis, stationary tests, and testing for multicollinearity, autocorrelation, and heterogeneity. The dataset of this study would be known as panel data or longitudinal data. There are various estimation techniques available to analyze panel data. However, this study focused on Fixed Effect/Random Effect panel regression. The model specifications of multiple regression of this study are as follows.

Model 1 and 2 (shareholder wealth and board structure)

Fixed effect

$$\text{Shareholder Wealth}_{it} = \beta_{0i} + \beta_1 (\text{SLS})_{it} + \beta_2 (\text{BSize})_{it} + \beta_3 (\text{NonEX})_{it} + \beta_4 (\text{WomB})_{it} + \beta_5 (\text{Lev})_{it} + \beta_6 (\text{FSize})_{it} + u_{it}$$

Random effect

$$\text{Shareholder Wealth}_{it} = \beta_0 + \beta_1 (\text{SLS})_{it} + \beta_2 (\text{BSize})_{it} + \beta_3 (\text{NonEX})_{it} + \beta_4 (\text{WomB})_{it} + \beta_5 (\text{Lev})_{it} + \beta_6 (\text{FSize})_{it} + u_{it}$$

Where:

Shareholder Wealth = the dependent variables of the study; it represents dividend yield and dividend per share for firm i at period t as an alternative estimation. β_0 = the constant term, β_{0i} = the y -intercept of firm i , $\beta_1 - \beta_6$ = the coefficients of the independent board composition related variables, i = listed firm, t = time or year, u_{it} = error term.

Validity and reliability of data

This research relied on secondary data. The information was gathered from the company's audited annual report and the Colombo Stock Exchange's guidebook. The data are extremely reputable and accurate because they have been audited and published by companies listed on Colombo Stock Exchange.

RESULT AND DISCUSSION

Descriptive statistics

The descriptive statistics pertinent to corporate governance practices and shareholder wealth are summarized in Table 1. The mean value of dividend per share is Rs. 4.208, which is declared annually by the companies listed on Colombo Stock Exchange in Sri Lanka. There is a huge variation in dividend declaration among companies, with the minimum value of Rs. 0.00, the maximum value of Rs. 75.00, and the standard deviation of dividend payment of companies was 9.705. It indicates that companies have a different type of dividend policy which has an impact on shareholders' wealth. The mean value of dividend yield was 0.032, which means that the investors are getting 3.2% of the return of investment annually. The maximum value of 76.5% and minimum value of 0.00% of dividend yield are recorded during the period. The standard deviation is recorded as 0.047, which implies a low variation of return on investment to the

shareholders. The average board size is eight directors, which are optimum number suggested by [Jensen \(1993\)](#).

Table 1. Summary of descriptive statistics

List of variables	Mean	Median	Maximum	Minimum	Standard deviation
Dependent variables					
Dividend per share (Rs.)	4.208	0.700	75.000	0.000	9.705
Dividend yield (Ratio)	0.032	0.024	0.765	0.000	0.047
Independent variables					
Board Size (Nos)	8.238	8.000	13.000	2.000	2.867
Separate leadership structure (%)	0.848	1.000	1.000	0.000	0.289
Non-executive directors (%)	0.476	0.423	1.000	0.000	0.243
Women on Boards (%)	0.075	0.000	0.556	0.000	0.171
Controlling variables					
Leverage (Ratio)	0.295	0.260	0.973	0.000	0.278
Firm size (Ln)	22.971	22.876	27.117	14.626	1.587

Source: the author (2022)

The minimum size of the Board of directors is reported as two, and the maximum number of directors was 15, which is similar to the recommendation of European and U.S codes for ideal board size. It is noted that 85% of the companies listed in Sri Lanka separated the position of CEO and Chairman of the Board, which is similar to the compliance of the code of best practices issued in 2013 (Section 1, Principal A.2). The proportionate of non-executive directors of listed companies in Sri Lanka is more than 2/3 of the total board size. It is reported that the composition of non-executive directors in the total board size is 47.6%. Additionally, it is proposed that companies must maintain gender balance in appointing the Board of directors, whereas it should be at least 35% of the total directors of the Board. The mean proportion of women participation on the Board was 7.5% which is less than the gender balance proposed by the experts. Other than the gender balance, the descriptive studies reveal that firms listed in Sri Lanka follow a code of best practices for developing corporate governance practices.

Spearman's correlation analysis

In order to test the relationship between Board structure-related variables and shareholder wealth of companies listed in Sri Lanka, Spearman's correlation

analysis was carried out in this study. The correlation matrix of the variables employed in this investigation is shown in Table 2.

Table 2. Spearman's correlation analysis

	DPS	DYD	Board size	Non-ExD	WOB	Leverage	FSize
DPS	1.0000						
DYD	0.3517	1.0000					
Board size	-0.1468	0.1340	1.0000				
Non-ExD	-0.2132	0.1467	-0.1590	1.0000			
WOB	0.1021	-0.0640	0.1302	-0.1425	1.0000		
Leverage	-0.1575	-0.0235	0.0456	0.0948	-0.1240	1.0000	
FSize	0.0521	0.0477	0.2438	0.1231	-0.0246	0.2314	1.0000

Source: the author (2022)

Note: DPS: Dividend per share, DYD: Dividend yield, Non-ExD: Non-executive directors, WOB: Women on Board, FSize: Firm size

During the period of research, board size and the fraction of non-executive directors are inversely connected with dividend per share and favourably correlated with dividend yield. The result is reported as a weak correlation between the variables. The representation of women on the Board leads to a positive correlation with dividend per share and a negative correlation with dividend yield. It presents the unit root test suggested by [Levin, Lin, and Chu \(2002\)](#) to test the stationarity of the data set. For all variables, the null of a unit is found to be rejected. At a 5% significant level, the LLC model confirmed that the variables are stationary.

Regression analysis

This study consists of two models in which model 1 is designed to assess the influence of Board structure-related variables on dividend per share (proxy to shareholder wealth), and model 2 is designed to predict the impact of board structure on dividend yield. The Breusch-Pagan Lagrange Multiplier test is summarized to determine whether or not the data exhibits a panel effect. The results of the Chi-square test for both models are highly high and statistically significant (p-value 0.05) at the 5% level. Since both models are significant, it is considered that the data contain a panel effect. As part of the pre-test, [Hausman's \(1978\)](#) test is carried out in this study to determine whether the models are fixed or have random effects. The Chi-square value demonstrates that the fixed effect belongs to model 1, and the random effect applies to model 2.

The regression analysis is shown in Table 3. F-test in regression findings indicates that models 1 and 2 provide a superior fit to the data, as their overall F-tests are statistically significant at the 0.0000 and 0.0156 (less than 5 per cent) levels, respectively. R^2 in regression model 1 accounts for 89.26% of the effect in variables, whereas R^2 in regression model 2 accounts for 12.41% of the effect in dividend per share and dividend yield (a proxy for shareholder wealth), respectively. Durbin Watson statistics are employed in this study to examine the autocorrelation in the residuals from models 1 and 2. Since the statistics account for 1.8 for model 1 and 1.5 for model 2, the test results suggest that there is no cause for autocorrelation. Variance Inflation Factors (VIF) are tested to detect the multicollinearity between the variables. Model 1 has a VIF statistic of 3.716, whereas Model 2 has a VIF statistic of 1.235, indicating that there is no multicollinearity between independent variables in the regression model. The findings of the Wald test of joint significance demonstrate that the factors utilized in this study can be used to predict the outcomes. According to the results of residual heterogeneity, there is no heteroscedastic problem in regression models 1 and 2, as revealed by the Breusch- Pagan- Godfrey test. Model 1's Theta (5.48) is lower than the chi-square test statistics of 15.61. (7d.f). Theta (6.17) is also less than the chi-square test results of 16.41 for model 2. (7d.f).

Table 3. Summary of regression analysis

Explanatory variables	Model 1		Model 2	
	Dividend per Share		Dividend Yield	
	Fixed Effect		Random Effect	
	Coefficient	P. Value	Coefficient	P. Value
C	1.4519	0.6372	0.0143	0.5614
Board size	0.0821	0.0275	0.0130	0.0363
Separate leadership	0.2773	0.0310	0.0121	0.0133
Non-executive director	1.4680	0.0049	0.0250	0.0185
Women on Board	2.1576	0.5277	-0.0241	0.2310
Leverage	-0.8479	0.5623	0.0234	0.8380
D (Firm size)	-0.1254	0.7526	0.0170*	0.0023
R-squared	0.8926		0.1241	
Adjusted R-squared	0.6473		0.0278	
S.E. of regression	4.453		0.1563	
F-statistic	16.385*		2.494*	
Durbin-Watson stat	1.814		1.489	
VIF	3.716		1.235	
Wald test	656.464*		225.655*	
Number of firms	175		175	

Number of observations	1050	1050
Source: the author (2022)		

Note: *5% significant level

S.E: Standard error, VIF: Variance inflation factors

Board size and its influence on shareholder wealth

The regression results in table 3 show the positive relationship between board size and dividend per share, and dividend yield in models 1 and 2, respectively. It implies that a larger board boosts shareholder wealth in Sri Lankan public firms. With a value of 0.0821 ($p = 0.0275 < 0.05$), the correlation between board size and dividend per share is statistically significant. As for model 2, the relationship between board size and the dividend yield is also reported to be statistically significant with a coefficient of 0.0130 ($p = 0.0363 < 0.05$). Therefore, based on the significant relationship between board size and shareholder wealth in models 1 and 2, the null hypothesis of the first research hypothesis (H_1) is rejected, and it can be concluded that board size does bring benefits to listed companies in Sri Lanka to increase shareholder wealth.

The findings of the study related to board size and shareholder wealth of listed companies in Sri Lanka support the findings of previous research and the prediction of agency theory. [Jensen and Meckling \(1976\)](#) state that the Board of directors plays an important role and governs the function of the Board to monitor management action to enhance shareholder wealth. It can be achieved through the effectiveness of the Board and its size. Board size determines the shareholder wealth in which a larger board is preferable to maximize shareholder wealth where the experience and expertise of the directors will add value to the firm ([Floracking, 2008](#); [Prempeh and Odartey-Mills, 2015](#); [Singh and Davidson, 2003](#)). The result of this study is consistent with the agency and resource dependence theories, which predict that a firm having a larger number of directors would be effective in enhancing shareholder wealth. [Kiel and Nicholson \(2003\)](#) state that to overcome the conflict of interest between management and shareholders, a bigger number of directors would be an effective corporate governance mechanism.

The finding of this study is, however, in contrast to the view of [Kalainathan and Vijayarani \(2014\)](#) and [Dissabandra \(2012\)](#), which criticized the Board of directors and their role in solving the agency problem of the companies. In addition, the evidence of the previous study reveals that the size of the Board does bring clear benefits to shareholders. It is noted in this study that the Board of directors can monitor the management action and solve agency problems of listed companies in Sri Lanka. It shows the real application of the agency and

resource dependency theories which led the policymakers and practitioners to follow the guidelines of the theories when planning the size of the Board in the future.

Separate leadership structure and its influence on shareholder wealth

The results indicate that separating the position of Chief Executive Officer (CEO) and Chairman of Board (COB) tends to increase the shareholder wealth of companies in Sri Lanka. It is reported that a positive relationship exists between separate leadership structure and dividend per share and dividend yield in models 1 and 2, respectively. The relationship between separate leadership structure and dividend per share is statistically significant, with a coefficient of 0.2773 ($p = 0.0310 < 0.05$). A significant relationship is also reported between separate leadership structure and dividend yield with a coefficient of 0.0121 ($p = 0.0133 < 0.05$). Since both models are statistically significant, the null hypothesis of the second research hypothesis (H_2) is rejected. Therefore, it proves that separate leadership structure influences maximizing shareholder wealth of listed companies in Sri Lanka.

The findings on the relationship between separate leadership structures and shareholder wealth are supported by agency and resource dependency theories as well as the code of best practice of corporate governance issued in Sri Lanka. Corporate governance theories suggest separating the position of CEO and COB to avoid the domination of the management on board function. It is observed that 85 per cent of listed firms in Sri Lanka have separate leadership structures that adhere to the code of corporate governance best practices issued to Sri Lankan companies. It is also in line with the suggestion given by [Code \(1992\)](#) and [Jensen \(1993\)](#). This implies that the separate leadership structure does perform better due to the ability of the Chairman to determine strategies suited to the business environment.

Non-executive directors and their influence on shareholder wealth

Statistical analysis of the relationship between non-executive directors and their influence on shareholder wealth reported significant results. The results show a positive relationship between non-executive directors on Board and dividend per share and dividend yield in models 1 and 2, respectively. The relationship between non-executive directors on the Board and dividend per share is significant, with a coefficient of 1.4680 ($p = 0.0049 < 0.05$). Also, the relationship between the representation of non-executive directors on the Board and the dividend yield is significant, with a coefficient of 0.0250 ($p = 0.0185 < 0.05$).

However, based on the significant relationship reported in both models (1 and 2), the null hypothesis of the third research hypothesis (H_3) is rejected. Therefore, there is evidence to accept the alternative hypothesis, which means that separate leadership structures influence the shareholder wealth of listed firms in Sri Lanka.

As far as shareholder wealth is concerned, the Board of listed companies should have a balance of executive and non-executive directors on the Board to take rational and moral decisions (Kiel and Nicholson, 2003), which is based on the information and resources brought by the majority of non-executive directors to the board meetings (McKnight and Weir, 2009). It is noted that the proportion of non-executive directors on the Board of listed companies in Sri Lanka is 48 per cent which is closer to the U.K. code of best practice of 49.5%. The code of best practice also suggests having non-executive directors 2/3 of the total board size. It is pointed out that a higher proportion of non-executive directors on the Board are more effective in monitoring management action to enhance shareholder wealth (Florackis, 2008; Garanina and Kaikova, 2016).

The evidence of this study supports the above arguments and as well as the prediction of agency theories which propose that the Board of directors should consist largely of non-executive directors to maximize shareholder wealth (Fama and Jensen, 1983). Prior studies in this area reported that the majority of non-executive directors on the Board are considered important corporate governance mechanisms to maximize shareholder wealth (Gul et al., 2012; Kiel and Nicholson, 2003; Reddy and Locke, 2014; Roudaki and Bhuiyan, 2015). Reddy and Locke (2014) further state that the proportion of non-executive directors influences shareholder wealth. It seems that non-executive directors have multiple skills required by the organization. This meant that the Board's independence ensured that listed firms in Sri Lanka followed good corporate governance practices to maximize shareholder wealth.

Women on Board and their influence on shareholder wealth

The influence of women's representation on the Board on shareholder wealth of companies listed in Sri Lanka is reported as insignificant results in both models (1 and 2). The results of model 1 indicate a positive relationship between women's participation on Board and dividend per share, which is insignificant with a coefficient of 2.1576 ($p = 0.5277 > 0.05$). A negative relationship is reported in model 2, which is insignificant between women on board and dividend yield with a coefficient of -0.0241 ($p = 0.2310 > 0.05$). Therefore, based on the insignificant relationship between the variables, the null hypothesis of the

last research hypothesis (H₄) is not rejected. There is no evidence to accept the alternative hypothesis. It can be concluded that the participation of women on the Board does not influence on shareholder wealth of companies listed in Sri Lanka.

Gender diversity has been considered the main concern to the economic participation of women in the workplace, which is proposed by resource dependency theory. Gender diversity develops a broader network and resource base in the workplace to manage the firm efficiently and effectively and assist the managers in taking decisions rationally ([Singh and Davidson, 2003](#)). It has been noted that there is a trend of increasing women's participation in decision-making time ([Carter et al., 2003](#)). [Guy et al. \(2011\)](#) found that women's participation on a company's Board has a direct impact on firm performance. The study reveals that shareholder wealth could be maximized through gender diversity. A diverse board tends to enhance shareholder wealth to resolve conflicts of interest.

The results of this study regarding women's participation on companies' boards are inconsistent with the theoretical expectation, which proposes a higher number of female representations on Board (diverse Board) that tends to protect the interest of shareholders. The findings of this study indicate that the proportion of women on the Board is not associated with shareholder wealth. The reason for this finding is the lowest ratio of (7.5 per cent) women representation on companies' boards in Sri Lanka which does not meet the theoretical expectation. [Kanter \(2008\)](#) states that female participation on Board must be at least 35% of the total board size. Compared to other countries, [Adams and Ferreira \(2009\)](#) report that the composition of female directors on companies' boards in Australia, France, Europe, Sweden, and Norway is 8.3%, 7.6%, 9.7%, 26.9%, and 44.2%, respectively. [Garanina and Kaikova \(2016\)](#) also report that proportion of female directors on the Board is 50% in Norway, 18% in the USA, and 10% in Russia. In Norway, there is a quota system implemented for women to take part in companies' boards which is the reason to have the higher proportion. This implies that there is room for the development of board diversity in listed firms in Sri Lanka.

CONCLUSION

This study investigates the impact of Board composition-related variables on shareholder wealth of companies listed in Sri Lanka through the lens of agency and resource dependency theory. Corporate governance-related theories such as agency theory and resource dependency theory propose best practices on

corporate governance mechanisms to resolve agency problems. The companies listed in Sri Lanka were required to adopt corporate governance best practices to protect the interest of shareholders. Researchers pointed out that existing corporate governance practices in Sri Lanka are not up to the standard, and there is a weakness in companies' board function and leadership structure. In the meantime, it is noted that companies were progressing well, and the stock market was also well-performing. It raises serious questions about the protection of shareholder wealth in listed firms in Sri Lanka.

This research studied the correlation between Board structure-related variables such as board size, separate leadership structure, the proportion of non-executive directors and women on the Board, and shareholder wealth. The findings indicate that board size, distinct leadership structure, and the number of non-executive directors on the Board affect shareholder wealth positively and considerably. It is noted that a larger board and a higher proportion of non-executive directors on the Board would be benefited, shareholders. A larger number of directors and a higher proportion of independent directors increase shareholder wealth which supports the theoretical prediction of agency and resource dependency theory, while a separate leadership structure also tends to enhance shareholder wealth of companies listed in Sri Lanka. The findings related to women's participation on boards do not have any significant influence on shareholder wealth. The reason for the insignificant relationship was that women were not given prominence in the business of the companies.

The evidence indicates that present corporate governance practices are consistent with agency and resource dependency theories and the Sri Lankan code of best practices for corporate governance. The Board structure-related variables are most important and tend to protect the best interest of shareholders. It informs the policymakers and practitioners on gender diversity in board affairs. It also provides useful information to develop a framework for the inclusion of more female directors in company affairs. Due to time constraints, this study did not include all corporate governance measures offered in codes of best practices and theories. This study focused on listed companies in Sri Lanka which cannot be generalized to non-listed companies or private companies. This study can be extended to non-listed companies and also to the bank and financial institutions which has unique ownership and governance structure in the future.

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