

HEIDRICK & STRUGGLES

Corporate Governance Report **2011**

Challenging board performance

South Africa

Supplement to the European Report

Foreword

Following our well-received 2009 publication, *Boards in turbulent times*, Heidrick & Struggles, has again, examined the status of the largest South African public companies with respect to global corporate governance practices, and compared them specifically with the top public companies of fifteen European countries.

The findings are all the more relevant against the backdrop of the country's growing role as an emerging market, and its position as the springboard for global enterprises' growth strategies into Africa. It should be noted that South African boards have suffered the same erosion of public trust and tolerated increased scrutiny regarding their performance and governance, as have their global counterparts.

The topic of leadership and leadership practices has dominated South African headlines for the past year. The launch of this 2011 publication, *Challenging Board Performance*, comes at an appropriate time to contribute to the national debate.

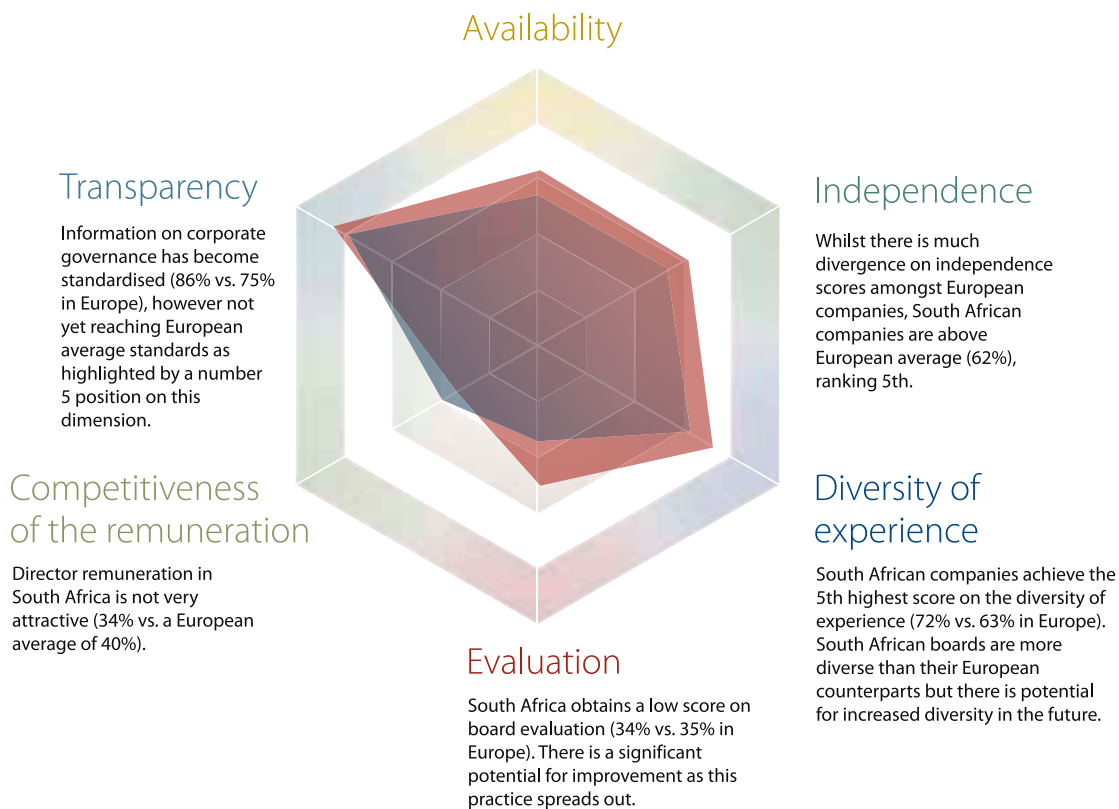
figure 1

The state of corporate governance in South Africa and Europe

(see Table 1 for more detail)



South African companies achieve the 2nd highest score on directors' availability (63% vs. 54% in Europe).



South African overview

Our report highlights the current state of corporate governance practices in South Africa and covers six key areas: availability, independence, diversity of experience, evaluation, competitiveness of remuneration and transparency (*fig 1*).

Unlike their European counterparts, South African boards are under constant pressure to increase levels of racial diversity to address historical inequalities and to conform to the requirements of Broad Based Black Economic Empowerment legislation. The impact of these pressures is ever evident and suggests that there has to be earlier investment in mentoring leadership talent.

The greatest concern that South African directors faced related to the fact that they served on a greater number of boards than their European counterparts. And that even though South African boards met somewhat less frequently, the number of committee meetings was notably higher, at 19 per year. This confirmed a trend our Board Effectiveness practice was observing in South Africa – that much of the substantive work of boards had shifted to committees.

However, we found the communication from committees back to the main board was less than optimal and there needed to be an increased focus in service of good governance practices.

Further progress had been made over the last two years on two fronts: 80% of boards have completed board evaluations, an increase from 68% in 2009. Secondly, the number of women on South African boards remains somewhat ahead of Europe at 14.5% vs 12.1%; and one-third of boards are comprised of at least 20% women.

Methodology

Our biennial corporate governance report is based on the analysis of the 2010 annual reports of the top public companies in 15 European countries. This supplement compares the South African top 40 companies on the Johannesburg Stock Exchange (JSE) as at the end of June 2010 against the European results.

In this report, we developed an approach to reviewing board effectiveness, which we structured around three areas of risk and underperformance: (1) Process and Structure (2) Profiles and Competencies of directors, and (3) Culture, Behaviours and Team Dynamics.

1 Process and Structure

Notable trends

South African boards still meet less frequently at 6.8 times a year vs the European average of 9.4 (*table 1*). However, there are nearly 19 committee meetings per year, which is amongst the highest number (only in the UK are there more). One of the reasons for the high number of meetings is the increasing number of committees per board: 4.4 vs a European average of 3 (*table 2*). Thirty-five percent of South African companies have 5 committees or more.

All companies have audit and remuneration committees; 95% have nomination committees. South Africa has the highest prevalence of ethics and corporate social responsibility committees with 60% vs a European average of 12%, 85% vs 15% in Europe of risk committees and the second highest proportion of governance committees after Portugal with 55% vs 21% in Europe (*table 3*).

Progress since 2009

As mentioned above, there has been progress on board evaluations, with 82% of the South African companies reporting that their boards conducted evaluations – significantly higher than 68% in 2009. This is higher than the European average of 75% (*table 4*).

In two thirds of the cases, the individuals conducting the process were independents. External consultants are involved in 41% of cases. Non-independent evaluations were led by Chairmen 25%, committees 19% and lead directors 6%.

The evaluation method has also become more sophisticated with only 20% of evaluations based on questionnaires and 80% of evaluations comprised of interviews that were sometimes accompanied by questionnaires. 84% of evaluations include individual evaluations of directors.

Disclosure of corporate governance mechanisms is generally good. Companies in South Africa are at or above European standards on all criteria except: disclosure of start and end of tenure at 25%; director remuneration structure at 65%; and the reporting of committee activities at 78%.

The South African analysis showed improved compliance levels with 68% of companies stating that they fully comply with the national corporate governance code, which is higher than the European average of 55% but somewhat lower than the UK.

About one in four South African companies hold a strategy day, which is greater than the European number.

Areas for attention and improvement

At 6.8 meetings per year vs a European average of 9.4, the frequency of board meetings is the second lowest number compared to Europe. Surprisingly this number has not increased over the years.

A review of the average number of directorships that are held concurrently by directors and chairmen, showed that South African directors tended to be slightly less available than their European counterparts and chairmen more available (*fig 2*).

Comparable with Europe

All South African companies in our analysis have a full unitary board structure similar to that which is found in the UK.

93% attendance is the same as the European average.

The average age of directors remains unchanged at 56.5 years, about 2 years younger than the European average.

2 Profiles and Competencies

Comparable with Europe

With a stable 14.5% of female directors, the proportion of gender diversity in South Africa is marginally above the European results level of 12.1% (*table 5*). One-third of boards consist of at least 20% of women and 15% of boards are comprised of men only.

Areas for improvement

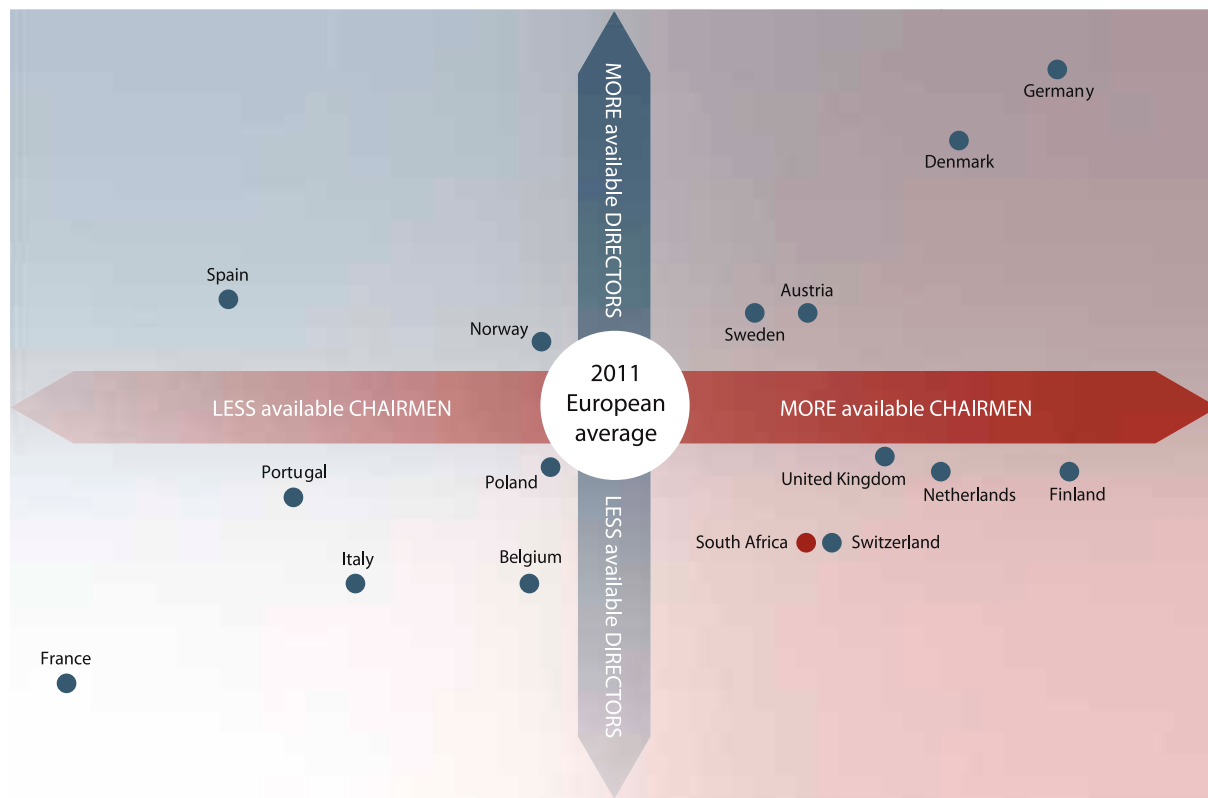
Functional diversity is more important than ever before and there should be a core group of directors with specific industry or functional knowledge. 65% of audit committees comprise a CFO – current or former – or a chartered accountant, which is below the European average of 72%. Three-quarters of boards comprise a director with some legal expertise, half of which hold legal portfolios. One-third of board members are current or former CEOs, with CEO representation below that which we found in Europe at 43%.

If companies are to expand globally, internationalisation of South African boards is important. There was a slight improvement on this indicator, as 28% of directors are non-nationals (up from 23% in 2009). However, there could be more diversity in the nationalities represented on the board as half of all foreign directors are British (*table 6*).

figure 2

Chairman and director availability

(based on average number of executive positions and non-executive positions in public companies)



3 Culture, Behaviours and Team Dynamics

In the European report, most of this section focuses on our points of view including recommended best practices, and only a small portion of the content is derived from the analysis of statistics. However there were notable trends emerging around the chairman profile (table 7).

In all South African companies reviewed, chairmen and CEO roles were split. 28% of chairmen moved to this role upon retirement as CEO. This does not accord with international best practices.

Only 45% of chairmen are independent vs 73% in the UK.

Conclusion

While recognising the progress noted above, there is much work to be done to elevate the practices of South African companies to the European and global standards. Issues around competencies – functional diversity, background and independence – need to be addressed very deliberately in the renewal of boards.

We also believe that it is imperative for companies to invest early in the development of skills for new directors, and so expand the pool of available talent nationally. Providing mentorship and exposure to experienced directors and chairmen will help build successive generations of accomplished business leaders.

Tabular data

	Austria	Belgium	Denmark	Finland	France	Germany	Italy	Netherlands	Norway	Poland	Portugal	South Africa	Spain	Sweden	Switzerland	United Kingdom	2011 European average
table 1 Frequency of board meetings																	
Average number of full board meetings per year	6.0	8.0	9.1	11.4	9.0	5.9	11.3	8.3	14.2	9.2	8.9	6.8	10.9	10.3	8.4	9.4	9.4
% of companies organising a strategy away day	20	20	21	n/a	35	13	n/a	56	35	n/a	n/a	28	9	22	20	29	19
table 2 Average number of board committees																	
Average number ▲ denotes increase on 2009	2.7 ▲	3.0	2.3	2.2 ▲	3.4	4.5 ▲	2.3 ▲	3.2	2.1 ▲	n/a	3.0 ▲	4.4	2.9	3.2 ▲	3.6	3.9 ▲	3.0
table 3 Prevalence of board committees																	
% with Audit	100	100	95	96	100	97	98	100	100	89	85	100	100	100	100	100	98
% with Remuneration	85	90	58	95	98	90	95	96	75	58	100	100	100	93	100	100	91
% with Nomination	70	95	11	58	95	93	30	96	15	16	25	95	100	100	80	100	71
% with combined Remuneration & Nom.	35	70	0	46	53	0	10	20	0	11	20	15	100	0	30	0	27
% with Strategy	25	30	11	0	58	30	5	16	0	26	0	13	14	0	5	0	15
% with Ethics and social responsibility	0	5	0	0	20	7	0	12	10	5	20	60	3	0	10	53	12
% with Governance	0	15	0	8	38	40	13	24	10	21	60	55	9	4	60	16	21
% with Risk	10	10	21	13	15	17	3	12	0	11	20	85	14	11	30	29	15
table 4 Boards undertaking evaluation between 2008 and 2010																	
% of boards undertaking evaluation	70	60	95	95	95	60	70	88	60	58	40	82	89	93	25	98	75
table 5 Proportion of women on the board																	
% of board members are women	8	8	18	25	11	13	3	15	33	48	4	15	9	29	11	12	12
table 6 Non-national directors on the board																	
% of non-national directors	13	34	19	23	27	11	12	47	18	15	17	28	10	31	53	40	24
Average number of non-nationals	1	5	2	2	4	2	2	4	1	1	2	4	1	3	5	5	3
Average number of nationals	10	9	8	6	10	15	12	5	7	7	13	10	13	8	5	7	9
table 7 Chairman profiles in Europe																	
% Executive chairman / chairman and CEO	0	15	0	0	42	0	7	4	15	0	25	0	71	0	10	2	15
% Non-executive chairman is the former CEO	5	10	21	25	30	60	10	4	5	5	25	28	11	26	30	10	19
% Non-executive non-independent chairman	50	50	58	25	13	23	73	20	40	48	25	27	12	52	30	15	33
% Independent non-executive chairman	45	25	21	50	15	17	10	72	40	47	25	45	6	22	30	73	33

How does your board compare?

To what extent do you agree with the following statements?

		<i>Strongly Disagree</i> > <i>Strongly Agree</i>				
		1	2	3	4	5
Process and Structure						
1	The mix of board competencies is adequate and allows directors to engage effectively with business issues and changing conditions	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
2	The board reviews top talent performance effectively and is appropriately engaged in succession planning	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
3	Board committees improve the overall effectiveness of the board	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
4	The board has the right level of exposure to the senior management cadre	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
5	Director commitment meets or exceeds expectation	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
6	The evaluation of board performance has delivered maximum value	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Profiles and Competencies						
7	The board has enough depth of experience to constructively challenge management	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
8	The board combines the necessary range of skills and perspectives required by the corporate strategy	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
9	There is a good balance between director independence and engagement with the management	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
10	The board's remuneration scheme for directors is attractive	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Culture, Behaviours and Team Dynamics						
11	The board operates with the optimum culture for its needs	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
12	The leadership style of the chairman encourages excellent team dynamics	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
13	The board dedicates enough time to identifying its own improvement opportunities	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Through our interviews with senior board members and corporate governance experts we identified 13 statements that are critical to consider when assessing board performance. **How does your board rate?**

HEIDRICK & STRUGGLES

Heidrick & Struggles is the leadership advisory firm providing senior-level executive search and leadership consulting services. For almost 60 years, we have been building deep relationships with the world's most talented individuals on behalf of the world's most successful companies. Through the strategic acquisition, development, and retention of talent we help our clients – from the most established market giants to the newest market disruptors – build winning leadership teams.

www.heidrick.com

South African supplement

This country supplement is an addition to the **2011 European Corporate Governance Report: Challenging Board Performance**. It is a study analysing how top public companies govern their boards, across 15 European countries and, for the first time, provides qualitative insights into the corporate governance landscape.

To order further copies of the full report and the **South African supplement**, please email cg2011@heidrick.com

For press enquiries please contact
emeamarketing@heidrick.com



Heidrick & Struggles South Africa

15th Floor – The Office Tower
Sandton City
PO Box 781213 – Sandton
Johannesburg 2146
South Africa

+27 11 685 6922

fax +27 11 685 6999

areesberg@heidrick.com

Copyright ©2011 Heidrick & Struggles International, Inc.
All rights reserved. Reproduction without permission is prohibited.
Trademarks and logos are copyrights of their respective owners.

201101PBTSSA63