Corporate Governance and Dividend Policy in Indonesian Manufacturing Companies

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Abstract. This study aims to examine the effect of corporate governance on dividend policy. The sample used in this study was 41 manufacturing companies listed on the Indonesia Stock Exchange for 2015 - 2019. The sampling technique used was purposive sampling, and the analysis method used was multiple linear regression. The independent variables in this study are board size, ownership structure (domestic institutional ownership and foreign institutional ownership), board independence, leverage, firm size, profitability, growth, free cash flow, liquidity, and capital expenditures.

Meanwhile, the dependent variable in this study is the dividend policy (dividend payout and dividend yield). The results showed that direct board independence, firm size, profitability, and growth positively affected dividend payout. Board size, leverage, and profitability significantly positively affect dividend yield. As moderating variables to assess ownership structure (domestic institutional ownership), capital expenditure and board independence significantly affect dividend payout. Capital expenditures have a significant negative impact on dividend yields. Board size, domestic institutions, foreign institutions, leverage, free cash flow, liquidity, and board independence as moderating variables to increase ownership structure (foreign institutions) do not affect dividend payout. Domestic institutional ownership, foreign institutional ownership, direct board independence, company size, company growth, free cash flow, liquidity, and board independence as moderating variables to increase ownership structure (domestic institutional ownership and foreign institutional ownership) do not affect dividend yields.

Keywords: Board size, ownership structure, board independence, leverage, firm size, profitability, growth, free cash flow, liquidity, and capital expenditures.

1 Introduction

Investors invest in a company to profit from dividends or capital gains [1]. The total amount of dividends the company distributes to investors depends on the policies set by the company [2,3]. A company can distribute dividends to investors when the company has good corporate governance, as in the previous research, which found that corporate governance has a significant positive effect on dividend policy in India [4]. If the company has good corporate governance, it will pay its investors dividends.

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Good company performance will increase the public's trust in the company, especially the shareholders; otherwise, if the company's performance is not optimal or wrong, the public and shareholder confidence in the company will also decrease [5]. Many board members in a company will affect dividend payments to investors. This is because if the company already has sufficient funds or even more to pay dividends, then the company will pay dividends to investors, whether the company has many boards of directors [4,6–8].

2 Hypothesis Development

The research in Indonesia found a strong correlation between board size and dividends, which justifies the importance of the board's role in promoting better corporate governance practices supported by the effectiveness of control by shareholders' dominant stock [4,6,9].

H1: There is an influence between board composition and dividend policy.

Ownership structure ratio of the number of shares owned by a person or institution or part of the management in the share ownership of a company [10–13].

H2: There is an influence between ownership structure on dividend policy

The ownership structure can still entrust its trust to the board of directors or commissioners. If there is an agency conflict, the ownership structures can discuss it directly with the existing agency agencies [4,12,14,15].

H3: There is an influence between board independence as a moderating variable on dividend policy

Companies that do leverage prove they are canine creditors to obtain cash flow that can be used to pay for their company's operating costs [4,16,17].

H4: There is an influence between leverage on dividend policy

The larger the company, the more often and consistently it will provide high dividends to its shareholders [4,18,19].

H5: There is an influence between firm size on dividend policy

The firms pay dividends to signal their firm value, and thus, profitable firms declare dividends to transmit this information to the market [7,17,20–22].

H6: There is an influence between profitability on dividend policy

The company is more likely to want to hold its profits for financing its operational activities and investment in the future rather than distributing these profits to shareholders as dividends [23–26].

H7: There is an influence between growth on dividend policy

The companies that can buy shares of other companies and become institutional owners at home and abroad will benefit from capital gains or dividend payouts [18,27–29].

H8: There is an influence between free cash flow on dividend policy

Companies that maintain a high liquidity scale will usually hold their earnings to finance future investments rather than paying dividends [4,23,30].

H9: There is an influence between liquidity on dividend policy

If the value of capital expenditure in a company decreases, it will affect the performance of the company, which will experience a decrease, not on dividend payout [23,24,31].

H10: There is an influence between capital expenditure on dividend policy

3 Methods

The sampling method used in this research is the purposive sampling method, which means that the withdrawal or sampling is determined by companies that have met specific criteria. The criteria for selection in this study include (1) Companies in the manufacturing industry listed on the Indonesia Stock Exchange from 2015 – 2019; (2) Companies that consistently issue dividends; (3) The company uses the rupiah currency. Forty-one manufacturing companies listed on the Indonesian Stock Exchange (IDX) were used in this study.

Below are the variables and measurements, also summarized in Table 1.

Table 1. Variables and measurements.

Variable	Symbol	Measure	Sign
Dependent:			
Dividend payout	DP	Dividend per share/ Earning per share	
Dividend yield	DIVY	Dividend per share/ Share price	
Independent:			
Board size	LBS	Ln total director	+
Ownership structure			
Domestic institutional investors	DIIOWN	% Domestic institutional investors	+
Foreign institutional investors	FIIOWN	% Foreign institutional investors	+
Moderating:			
Board independent	IND	Number of independent directors/ Total director	+
Control:			
Leverage	LIV	Total debt/ Total equity	-
Firm size	SIZE	Ln total assets	+
Profitability	ROA	Earning after tax/ Total asset	+
Growth	GROWTH	(Total asset $_t$ – total asset $_{t-1}$)/ Total asset $_{t-1}$	+
Free cash flow	FCF	OCF – NFAI – NCAI	+
Liquidity	LIQ	Current assets / Current liabilities	+
Capital Expenditure	CAPEX	Ln {(Total asset $_t$ – total asset $_{t-1}$)/ Total asset $_{t-1}$}	+

OCF = Operating cash flow
NFAI = Net fixed asset investment
NCAI = Net current asset investment

Multiple linear regression analysis was used as an analytical method in this study, with the following equation:

Model 1:

$$DPR = ß_0 + ß_1 DIIOWN + ß_2 FIIOWN + ß_3 IND + ß_4 LBS + ß_5 LIV + ß_6 SIZE + ß_7 ROA + ß_9 FCF + ß_{10} LIQ + ß_{11} CAPEX + ß_{12} DIIOWN^{*}IND + ß_{13} FIIOWN^{*}IND$$

Model 2:

$$DIVY = ß_0 + ß_1 DIIOWN + ß_2 FIIOWN + ß_3 IND + ß_4 LBS + ß_5 LIV + ß_6 SIZE + ß_7 ROA + ß_9 FCF + ß_{10} LIQ + ß_{11} CAPEX + ß_{12} DIIOWN^{*} IND + ß_{13} FIIOWN^{*} IND$$

4 Result and Discussion

4.1 Result

The descriptive statistic shows the mean, minimum, maximum, and standard deviation from 205 observations and all variables in Table 2.

Table 2. Descriptive statistics.

Variable	Mean	Minimum	Maximum	Std. Deviation
Dividend payout	.678009	-6.5415	25.2101	2.3322032
Dividend yield	.054952	.0010	1.9637	.1765785
Board size	1.635765	.6931	2.6391	.4581321
Domestic institutional investors	49.7361	.00	94.56	30.76698
Foreign institutional investors	21.3728	.00	93.00	28.77826
Board independent	.131486	.0000	1.0000	.1611135
Leverage	.878790	.0215	4.5469	.8510796
Firm size	12.666311	11.1264	14.5465	.7469761
Profitability	.095382	-.1240	.5267	.0959169
Growth	.117469	-.7621	1.1247	.1936313
Free cash flow	787.95	-18741	18745	3351.292
Liquidity	2.843018	.5842	21.7045	2.5660262
Capital Expenditure	29.165265	25.6195	33.4945	1.7199703

Based on the equations in Models 1 and 2, all results are shown in Tables 3

Table 3. T-test result.

Variable	Model 1		Model 2	
	Coefficient	P-value	Coefficient	P-value
Constanta	-0.700	0.042	0.066	0.036
Board size	0.035	0.478	0.016	0.001*
Domestic institutional investors	0.002	0.094***	-5.886	0.950
Foreign institutional investors	0.001	0.385	0.000	0.069***
Board independent	0.693	0.024*	0.020	0.494
Leverage	0.025	0.196	0.011	0.000*
Firm size	0.054	0.057***	-0.007	0.010*
Profitability	1.623	0.000*	0.114	0.000*
Growth	4.429	0.524	1.022	0.111
Free cash flow	2.179	0.643	4.926	0.255
Liquidity	0.013	0.045**	0.001	0.305
Capital Expenditure	-0.274	0.222	-0.043	0.038**
DOWN*IND	-0.006	0.159	0.000	0.328
FOWN*IND	-0.005	0.271	0.000	0.368

* Significances level of 0.03
** Significances level of 0.05
*** Significances level of 0.1

5 Discussion

Board size. In model 1, board size does not affect dividend payout. The results of this study are not in line with the research of [4,6], but the results of this study are in line with the analysis of [7]. In model 2, board size significantly positively affects dividend yield. This study's results align with research by [4,8]. With the increasing number of board sizes, the company can have more knowledge and information compared to only a few board sizes. If the company can develop for the better, then the company will get the opportunity to distribute dividends to investors.

Domestic institutional investors. In model 1, it is concluded that domestic institutional ownership has a significant positive effect on dividend payout. This study's results align with the research of [37]. When institutional ownership is high, the voice and support from institutions to control management are also higher. The impact is that management will provide excellent support to maximize the company's value so that the company's capacity will be maximized, which impacts shareholders getting dividends. In model 2, it is concluded that domestic institutional ownership does not affect dividend yield. This study's results align with the research of [4,38].

Foreign institutional investors. In model 1, it is concluded that foreign institutional ownership does not affect dividend payout. The results of this study are not in line with the research of [39,40], but the results of this study are in line with the analysis of [4,18]. In model 2, it is concluded that foreign institutional ownership has a significant positive effect on dividend yield. This study's results align with the research of [41]. Public companies prefer to pay dividends when their company has foreign institutional ownership.

Board independent. In model 1, it is concluded that an independent board positively affects dividend payout. This study's results align with the research of [42]. The more board independence, the more the company will pay dividends. Board independence reduces agency costs in the company and is more likely to represent shareholders effectively. In model 2, it is concluded that an independent board does not affect dividend yield. The results of this study are not in line with the research of [4], but the results of this study are in line with the analysis of [15].

Leverage. In model 1, it is concluded that there is no leverage effect on dividend payout. The results of this study do not support [16], but the results are in line with the research of [4,17]. In model 2, it is concluded that leverage positively affects dividend payout. This study's results align with the research of [15,42]. With the increasing number of funds from creditors obtained as leverage, the company can develop even better in the future by undergoing projects that can benefit the company and investors.

Firm size. In model 1, it is concluded that fit size positively affects dividend payout. The results of this study are in line with the research of [4,18,19]. In model 2, it is concluded that firm size has a negative impact on dividend yield. This study's results align with the research of [43]. The larger the size of a company, the more problems that the company will face will be even more significant, and the company will reduce the proportion of dividends distributed to investors.

Profitability. In models 1 and 2, it is concluded that profitability positively affects dividend policy. The results of this study are in line with [15,17,20–22]. Companies with high profitability will declare and pay higher dividends than companies not experiencing profits.

Growth. In models 1 and 2, it is concluded that firm growth does not affect dividend policy. The results of this study are not in line with the research of [23–26], but the results of this study are in line with the analysis of [4,35]. The faster the company grows, the more money it needs to finance its growth.

Free cash flow. In models 1 and 2, it is concluded that free cash flow does not affect dividend policy. The results of this study are not in line with the research of [18,27–29], but the results of this study are in line with the analysis of [4,44]. The company gets more free cash flow funds, so there is a possibility that the company can invest in many things.

Liquidity. In model 1, it is concluded that liquidity positively affects dividend payout. This study's results align with the research of [4,23]. Companies with a high level of liquidity illustrate that they can pay off all their short-term obligations, such as paying dividends or short-term debt. In model 2, it is concluded that there is no influence of liquidity on dividend yield. The results of this study are not in line with the research of [4], but the results of this study are in line with the analysis of [30].

Capital expenditure. Model 1 concludes that capital expenditure does not affect dividend payout. This study's results align with the research of [24,31]. Model 2 concludes that capital expenditure has a negative effect on dividend yield. This study's results align with the research of [23]. Companies that grow give lower dividends than companies that do not succeed because the retained earnings generated are mostly allocated for expansion or development in other parts, so the proportion of dividend distribution is reduced.

Board independence as a moderating variable of domestic institutional ownership on dividend yield. Models 1 and 2 conclude that domestic institutional ownership does not affect dividend policy through an independent board as a moderating variable. This study's results align with the research of [15,45]. The presence or absence of board independence will not affect dividend payments to investors. Suppose the company feels ready to pay dividends. In that case, the company will automatically pay dividends to investors so that investors continue to put their trust in the company and so that investors can raise capital for better company development in the future.

Board independence as moderating variable of foreign institutional ownership on dividend yield. Model 1 concludes that there is no effect of foreign institutional ownership through an independent board as a moderating variable on dividend policy. The results of this study are not in line with the research of [4,45], but the results of this study are in line with the analysis of [44], which states that board independence has no effect as a moderating variable for foreign institutional ownership on dividend payout. The ownership structure can still entrust its trust to the board of directors or commissioners.

6 Conclusion

In model 1, domestic institutional investors, board independence, firm size, and liquidity positively affect dividend payout. In model 2, the board size, foreign institutional investors, leverage, and profitability positively affect dividend yield. In contrast, the firm size and capital expenditure have a negative impact on dividend yield. The limitation of this research is in the methods, that is, multiple linear regression. The recommendation for the following study is to use panel data.

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