Do Ownership of Companies Effect to Financing and Dividend Policy?

Evidence from Indonesia Listed Non-Financial Industry Companies

Gary Lee, Yie Ke Feliana*, Stefanus Budy Widjaja Subali

University of Surabaya, Indonesia
**Corresponding author. Email: yiekefeliana@staff.ubaya.ac.id*

ABSTRACT
This study aims to determine the effect of ownership structure on financing and dividend policy. The ownership includes institutional ownership, managerial ownership, and concentration of ownership. Based on sample of 1.098 firm-years non-financial companies, the regression analysis shows that the higher the control by institutional owners, the lower company dividend rate are. However, managerial ownership does not affect the dividend and financing decision. On the other hand, concentrated ownership in a company increases company dividend rate and debt-financing. The results are robust whether the type of ownership and concentration ownership are test separately or simultaneously.

Keywords: *Institutional Ownership, Managerial Ownership, Concentrated Ownership, Financing Policy, Dividend Policy.*

1. INTRODUCTION

Company grows need capital, and capital come from primarily in the form of debt or equity. Each source of financing requires return in form of interest and dividend. Therefore, the financial management of company always include financing policy and dividend policy. These two policies are influenced by the shareholders because these need approvement in general shareholders meetings. Previous studies find that two types of shareholders that usually have strong control to the management decision is institutional shareholders and managerial shareholders itself (Haque et al, 2011; Mehrani et al., 2011; Sun et al, 2015; Boateng et al, 2017; Hunjra et al., 2020). In addition, in East Asia context, the ownership of companies tends to concentrate on the limited shareholders compare to the Anglo-Saxon companies (La Porta et al, 1998), therefore it is interesting to examine the effect of concentrated ownership on the financing dan dividend policy. Therefore, the purpose of this study is to examine the effect of institutional ownership, management ownership, and concentration of ownership on the financing and dividend policy.

2. HYPOTHESES DEVELOPMENT

The institutional owner with the large resources makes strengthen monitoring on the investee (Tayachi et al., 2021). The existence of institutional ownership in company reduces company risk and increase company credibility, as result reducing cost of debt that is offered by creditors. The debt financing decrease agency cost between management and shareholders due to reduce the available free cash for management opportunistic purpose (Hunjra et al., 2020).

H1: Institutional ownership increases company debt financing.

According to Jensen and Meckling (1976), managerial ownership aligns shareholders interest and management interests. Increase debt lead to increase monitoring by creditors, besides increase company financial risk (Brailsford et al, 2002). Therefore, management tends to do not use debt financing (Joher et al., 2006; Al-Fayoumi & Abuzayed, 2009).

H2: Managerial ownership reduces company debt financing.

Ownership concentration increases control power on management (Shleifer and Vishny, 1986; Khaw, 2019). The controlling shareholders prefer use debt than equity to prevent ownership dilution and maintain their control power (Sharofiddin et al., 2019). Although the debt increases company financial risk, the controlling shareholders think the

e-ISSN: 3047-857X

Proceedings of the International Symposium on Management (Volume 21, 2024)

dilution ownership is more important issues than the financial risk. They consider managing the financial risk is the management responsibility.

H3: Concentrated ownership increases company debt financing.

One type return to shareholders is dividend. With the tight monitoring on management, therefore it reduce the free cash flow available for management opportunistic purpose, the institutional shareholders tends to support dividend payment. This evidence was provided by Manos (2002); Chen et al. (2005), Thanatawee (2013); and Baitaineh (2020).

H4: Institutional ownership increases company dividend payment.

Management prefer to use internal fund than equity or debt financing due to lower cost of capital, as predicted by pecking order theory (Myers and Majluf, 1984). Th lower cost of capital makes increase profitability of company, in turn it leads to higher share price. Although the management has ownership in the company, the return that they will receive is higher in capital gain than in dividend. Jensen et al. (1992), and Nguyen and Vo (2014) research provide that evidence.

H5: Managerial ownerhsip reduces company dividend payment.

Concentrated ownership on limited shareholders provide opportunity for the controlling shareholders to expropriate company resources for their private benefits (Shleifer and Vishny, 1986). The controlling shareholders monitor management thightly thus they ask dividend payment in order to reduce free cash flow for management (Harada and Nguyen, 2011).

H6: Concentrated ownership increases company dividend payment.

3. RESEARCH METHOD

Population of this study is non-financial companies that are listed on Indonesia Stock Exchange during 2020-2021. Sample selection description is provided on Table 1. The operational definition of variable can be seen in Table 2.

Table 1. Sample Description

Description	Year		Total
	2021	2020	
Listed companies	771	825	1,597
Financial companies	105	105	210
Financial statement in other than IDR	90	92	182
Data for some variables are unavailable	51	55	106
Final sample	525	574	1,098

The hypotheses are tested using four regression models as follows (see Equation 1, Equation 2, Equation 3, and Equation 4).

$FP_{it} = \alpha_o + \alpha_1 IO_{it} + \alpha_2 MO_{it} + \alpha_3 P_{it} + \alpha_4 SZ_{it} + \alpha_5 G_{it} + \alpha_6 IC_{it} + \varepsilon_{it}$ ....(1)

$FP_{it} = \alpha_o + \alpha_1 OC_{it} + \alpha_2 P_{it} + \alpha_3 SZ_{it} + \alpha_4 G_{it} + \alpha_5 IC_{it} + \varepsilon_{it}$..............................(2)

$DP_{it} = \alpha_o + \alpha_1 IO_{it} + \alpha_2 MO_{it} + \alpha_3 P_{it} + \alpha_4 SZ_{it} + \alpha_5 G_{it} + \alpha_6 IC_{it} + \varepsilon_{it}$...........(3)

$DP_{it} = \alpha_o + \alpha_1 OC_{it} + \alpha_2 P_{it} + \alpha_3 SZ_{it} + \alpha_4 G_{it} + \alpha_5 IC_{it} + \varepsilon_{it}$.........................(4)

Table 2. Operational Definition Variables

Variables	Description	Measurement
Dependent variables		
FP_{it}	Financing Policy of firm i in year t	Total debt of firm i in year t, divided by total assets of firm i in year t
DP_{it}	Dividend Policy of firm i in year t	Total cash dividend of firm i in year t, divided by total net income of firm i in year t

Table 2. Operational Definition Variables (cont.)

Variables	Description	Measurement
Indepedent Variables		

IO_{it}	Institutional Ownership of firm i in year t	Total share owned by financial industries institution owner of firm i in year t, divided by total share issued and outstanding
MO_{it}	Managerial Ownership of firm i in year t	Total share owned by board of director of firm i in year t, divided by total share issued and outstanding
OC_{it}	Ownership Concentration of firm in in year t	Percentage ownership of the largest shareholder of firm i in year t
Control Variables		
P_{it}	Profitability of firm i in year t	Total net income of firm i in year t, divided by total assets of firm i in year t
SZ_{it}	Size of firm i in year t	Ln of total asset of firm i in year t
G_{it}	Growth of firm i in year t	Percentage of Change in Sales of firm i in year t compare to year t-1
IC_{it}	Interest Coverage of firm i in year t	Operating income of firm i in year t, divided by finance cost of firm i in year t

4. RESULT AND DISCUSSION

Regression results are reported on Table 3. Institutional ownership does not affect financing policy, although affect negatively to dividend policy, it means the results are rejected H1 and H4. The institutional owners seems do not interference to the management policy that does not effect directly to the shareholders. In this case, they do not interference the financing policy of management, but they take action about company devidend policy. However, the institutional owners decrease company dividend payout ratio, on contrary to the H4. This result is consistent to Kouki and Guizani (2009), and Johanes at al. (2021) findings. The reason of this result can be that the institutional owner is a long term investors that think more on company fundamental than just dividend that they can get shortly. While the descriptive analysis report that the means of growth is 74% per year, it means most of the sample firms experience high growth. The growth firms need more internal fund, and it makes reducing dividend payment capacity. The relation between growth, devidend, and institutional ownership are supported also in Huang and Paul (2016). Therefore, the higher institutional ownership makes reducing dividend payment.

Managerial ownership does not affect the financing policy and devidend policy, thus the results are rejected H2 and H5. The low managerial ownership in Indonesia companies, 8% in average, makes low control power on the financing and devidend policy. They are internal owner of the firm, therefore they

Concentration of ownership affect positively to the company financing and devidend policy, so H3 and H6 are accepted. As predicted, the controlling shareholders tends to reduce free cash flow in company. The purpose of this action to prevent opportunistic action of management. The positive effect of concentrated ownership to the debt financing policy is consistent to Khaw (2019) and Feng et al. (2020), while dividend policy is consistent to Nguyen and Harada (2011). In addition, for financing policy, the result supports that the controlling shareholder prevent to the ownership dillution.

All of these results are qualitatively consistent when institutional ownership, managerial ownership and concentration ownership are tested simultaneously. Due to limitation space, the regression results are not reported.

The results of control variables are mainly as predicted. Profitable company reduce the debt financing due to availability of internal fund, while increase the devidend payment. Larger firms tend to use debt financing and have higher devidend payment due to the capacity that they have. Interest coverage variable has only significant effect on the financing policy, but has not effect on devidend payment. Last, company growth does not influence financing and devidend policy.

Table 3. Regression Results

Variables	Model 1: FP Coeficient (p value of t test)	Model 2: FP Coeficient (p value of t test)	Model 3: DP Coeficient (p value of t test)	Model 4: DP Coeficient (p value of t test)
Constant	-0.734 (-6.809)*	-0.783 (-7.670)*	-0.773. (-7.586)*	-0.767 (-8.026)*
IO_{it}	0.020 (0.545)		-0.093 (-2.617)*	
MO_{it}	-0.026 (-0.671)		-0.019 (-0.514)	
OC_{it}		1.114		0.079

		(3.603)*		(2.671)*
P_{it}	-1.2 (-15.614)*	-1.268 (-16.776)*	0.059 (2.854)*	0.036 (2.215)*
SZ_{it}	0.043 (11,140)*	0.042 (11.576)*	0.032 (8.828)*	0.030 (8.665)*
G_{it}	0.001 (1.253)	0.001 (1.270)	-0.001 (-0.982)	-0.001 (-0.918)
IC_{it}	-6.488E-6 (-2.066)*	-6.688E-6 (-2.163)*	5.406E-6 (1.752)	5.319E-6 (1.771)
F test (sign.)	55.246 (<0,000)	74.433 (<0.000)	20.181 (<0.000)	22.304 (<0.000)
Adjusted R^2	0.240	0.262	0.096	0.090
N	1,032	1,035	1,086	1,080
H	H1 & H2: Rejected	H3:accepted	H4 & H5: rejected	H6:accepted

Note:* significance at 5%

5. CONCLUSION

This study finds that debt financing policy of company is influenced positively by concentrated ownership. The devidend policy of company is influence negatively by institutional ownership and positively by concentrated ownership. These results show that institutional owner is a long term investor, and controlling shareholder maintain their power by supporting debt financing and devidend payment.

This study contribute to development of literature in relationship between financing and devidend policy in one hand, and ownership in another hand. Specifically, this study provides more evidence under East Asian countries context where have higher concentration of ownership relatively to the other region.

REFERENCES

AL-Fayoumi, N., & Abuzayed, B. (2009). Ownership structure and corporate financing. Applied Financial Economics, Vol. 19 No.24, pp. 1975-1986. doi:10.1080/09603100903266807

Baitaineh, H. (2020). The impact of ownership structure on dividend policy of listed firms in Jordan. Cogent Business and Management, Vol. 8 No.1, pp. 1-18.

Boateng, Franklin, Ngwu, Xiaogang, Daniel, Bi, . . . Agyenim. (2017). The influence of internal corporate governance mechanism on capital structure decisions of chinese listed firms. Review of Accounting and Finance, 444-461. doi:10.1108/RAF-12-2015-0193

Brailsford, T., Oliver, B., & Pua, S. (2002). On the Relation between ownership structure and capital structure. Accounting and Finance, Vol. 42 No. 1, pp. 1-26. doi:10.1111/1467-629X.00001.

Chen, Z., Cheung, Y., Stouraitis, A., & Wong, A. (2005). Ownership concentration, firm performance, and dividend policy in Hong Kong. Pacific-Basin Finance Journa, Vol. 13 No. 4, PP. 431-449.

Feng, Y., Hassan, A., & Elamer, A. A. (2020). Corporate governance, ownership structure and capital structure: evidence from Chinese real estate listed companies. International journal of accounting & information management. doi:10.1108/IJAIM-04-2020-0042

Harada, K., & Nguyen, P. (2011). Ownership concentration and dividend policy in Japan. Managerial Finance, Vol. 37 No.4, pp. 361-376.

Haque, F., Arun, T., & Kirkpatrick, C. (2011). Corporate Governance and Capital Structure in Developong Countries: a case study of Bangladesh. Applied Economics, Vol. 43 No. 6, pp. 673-681. doi:10.1080/00036840802599909.

Huang , W., & Paul, D. (2016). Institutional Holdings, Investment Opportunities and Dividend Policy. The Quarterly Review of Economics and Finance, pp. 1-33. doi:http://dx.doi.org/10.1016/j.qref.2016.06.008

Hunjra, A. I., Perveen, U., Li, L., Chani, M. I., & Mehmood , R. (2020). Impact of Ownership Concentration, Institutional Ownership and Earnings Management on Stock Market Liquidity. Corporate Ownership and Control, Vol. 17 No .2, pp. 77-87. doi:10.22495/cocv17i2art7.

Jensen, M., & Meckling, W. (1976). Theory of The Firm: Managerial Behaviour, Agency Cost and Ownership Structure. Journal of Financial Economics, 305-360

Johanes, S. R., Hendiarto, R., & Nugraha, M. N. (2021). The Effect Of Institutional Ownership, Managerial Ownership, And Company Size To Dividend Policy. International Journal of Trends in Accounting Research, Vol. 2 No.1, pp. 88-93

Joher, H., Ali, M., & Nazrul, M. (2006). “The impact of ownership structure on corporate debt policy: two-stage least square simultaneous model approach for post-crisis period: evidence from Kuala Lumpur stock exchange. International Business and Economics Research Journal (IBER), Vol. 5 No. 5, pp. 51-63. doi:10.19030/iber.v5i5.3480.

Khaw, E. (2019). Debt financing puzzle and internationalization. Journal of Asia Business Studies, Vol. 13 No. 1, pp. 29-52La Porta, F Lopez-de-Silanes, A Shleifer, RW Vishny (1998). Law and Finance. Journal of political economy 106 (6), 1113-1155

Kouki, M., & Guizani, M. (2009). Ownership structure and dividend policy evidence from the Tunisian stock market. European Journal of Scientific Research, Vol. 25 No.1, pp. 42-53.

Porta, R. L., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. W. (1998). Law and finance. Journal of political economy, 106(6), 1113-1155.

Manos, R. (2002). Dividend policy and agency theory: evidence on Indian firms. Institute for Development Policy and Management, Vol. 16 No. 1, pp. 138-150.

Mehrani, S., Moradi, M., & Eskandar, H. (2011). Ownership structure and dividend policy: Evidence From Iran. African Journal of Busines Management, Vol. 5 No. 17, pp. 7516-7525. doi:10.5897/AJBM11.468

Myers , S., & Majluf , N. (1984). Corporate financing and investment decisions when firms have information that investors do not have. Journal of Financial Economics, Vol. 13 No.2, pp. 187-221.

Nguyen , V. T.-Y., & Vo, D. H. (2014). Managerial Ownership, Leverage and Dividend Policies: Empirical evidence from vietnam's listed firms. International Journal of Economics and Finance, Vol. 6 No. 5, pp. 274-281. doi:doi:10.5539/ijef.v6n5p274

Tayachi, T., Hunjra, A. I., Jones, K., Mehmood, R., & Al-Faryan, M. A. (2021). How does ownership structure affect the financing and dividend decision of firm? Journal of Financial Reporting and Accounting, Vol. 21 No.3, pp. 729-746.

Sharofiddin, A., Husin, M. M., Othman , A. H., Nomran, N. M., & Haron , R. (2019). The influence of firm, industry and concentrated ownership on dynamic capital structure decision in emerging market. JOURNAL OF ASIA BUSINESS STUDIES, vol. 15 No.5, pp. 689-705.

Shleifer , A., & Vishny, R. W. (1986). Large Shareholders And Corporate Control. The journal of political economy, Vol. 93 No.3, pp. 461-488.

Sun, J., Ding, L., Guo, J. M., & Li, Y. (2015). Ownership, capital structure and financing decision : evidence from the UK. British Accunting Review, Vol. 48 No. 4, pp. 448-463. doi:http://dx.doi.org/10.1016/j.bar.2015.04.001

Thanatawee, Y. (2013). Ownership Structure and Dividend Policy: Evidence from Thailand. International Journal of Economics and Finance, Vol. 5 No. 1, pp. 121 – 129.