

Firm Profitability, Ownership Structure and Dividend Policy on the Indonesian Manufacturing Companies

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ABSTRACT

This paper aims to investigate the relationship between firms' profitability and the level of insiders' ownership, government ownership, and foreign ownership and its effect on the dividend distribution for manufacturing firms in Indonesia over the period of 2009 to 2015. Two main proxies were employed for a firm's profitability: (namely) return on asset (ROA) and net profit margin (NPM). Using panel data regression, the results revealed that profitability had a positive impact on dividend distribution; this finding supports dividend-signaling theory. The association between dividends and insiders' ownership was consistently negative, but not significant. Thus, the cash flow expropriation by insiders at the cost of minority shareholders was not proven in this study. However, this early warning signal must serve as an alarm for the regulators, even though, not all public listed firms were examined in this study. Furthermore, the higher government ownership resulted in an increase in dividend payment, thus political factors and cash needed to fund country budget might influence this decision. This study also found a negative relationship between the level of foreign ownership and dividend payment, so when firms cut dividend

payments, it serves as a signal to the market that foreigners are not tunneling cash to its principal abroad. These results are expected to raise concern regarding corporate governance issues, especially regarding minority shareholder protection.

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INTRODUCTION

Earlier dividend payout studies viewed dividends as a form of distribution profit used to communicate information to shareholders as well as to meet the demand payment from diverse types of clientele (Allen & Michaely, 2003; Denis et al., 1994). However, De Angelo et al. (2004) found that clientele did not have a major impact on other circumstances in the decade after year 2000. Aggregate dividends supply increases as the aggregate earnings of a small number of companies in the United States (US) increases. De Angelo et al. (2006) confirmed that the firm profits or capital mix became dominant determinant factors in firms' dividend policy, thus providing support for the life-cycle theory of dividends.

De Angelo et al. (2006) combined the life-cycle theory and agency theory with the free cash flows theory from Jensen (1986) as well as firms' investment opportunity (Fama & French, 2001) and predicted that firms would adjust their dividend payment over time in response to the advancement of their opportunity set. The free cash flow theory and its relation to dividend payment, proposed by Jensen and Meckling (1976), was in line with this philosophy. When there are no attractive investment opportunities, in an effort to minimize conflict of interest between managers and shareholders, firms tend to distribute their profit or their excess cash flows to shareholders. Some researchers then tested this theory and confirmed that a company's profitability played a significant role in dividend policy. Among these

researchers were Chang et al. (2016); Fama and French (2002) who analyzed US data. Empirical evidence in emerging countries supports these results, with findings from countries such as Ghana (Amidu & Abor, 2006), Korea (Hwang et al., 2013), some African countries (Jabbouri, 2016) and Indonesia (Mulyani et al., 2016).

Dividends are also used to prevent managers from expropriating the firm's cash flow for unprofitable investments or other personal interests (Jensen & Meckling, 1976). Additionally, this dividend payout functions to discipline managers by reducing the amount of available internal cash flows; thus, they are compelled to look for other funding alternatives, such as external financing, which is controlled strictly by creditors (Easterbrook, 1984).

Dividend payments can be viewed as a transfer of wealth from the majority shareholder to another minority shareholder (La Porta et al., 2000). Large controlling shareholders such as institutions, families, or state enterprises may create an agency conflict with minority shareholders that have different magnitudes of interest. Majority shareholders then withhold dividends to expropriate minority shareholders for their private benefit (Gugler & Yurtuglu, 2003). However, Villalonga and Amit (2006) explained that the classic agency problem could be mitigated through concentrated ownership that instilled power to control managers. Thus, it can be said that the ownership structure affects dividend payout policy. Chang et al. (2016) and Firth et al. (2016) showed that there was a

positive relationship between the institution ownership and the portion of dividend payout. Meanwhile, Mulyani et al. (2016) pointed out that public listed companies in Indonesia controlled by the majority of the founding families paid relatively small dividends to their shareholders.

This study aims to reexamine whether the level of ownership structure and profitability of public manufacturing companies in Indonesia affect the dividend payout policy. This topic is motivated to be explored for several reasons. First, few articles have been published that discuss dividend policy for Indonesian companies. Among them, Mulyani et al. (2016) and Setia-Atmaja et al. (2009) analyzed the effect of family ownership on dividend payout policy. Second, Indonesia applies different rules and regulations on the protection of shareholders as well as different tax laws with other countries that will impact dividend policy (La Porta et al., 2000). Third, the manufacturing industry plays a fairly central role in contributing to the Indonesian economy, whose share of the GDP is about 21%. The industry's share of contributions to the GDP has decreased in recent years, thus it would be interesting to examine the dividend policy in the industrial sector in terms of ownership and profitability.

This study contributes to the literature by updating and increasing the understanding of dividends policy and its relationship to the level of ownership and a firm's profitability in the Indonesian capital market. In contrast to Mulyani et al. (2016) and Setia-Atmaja

et al. (2009), who reviewed the effect of family ownership and dividend payment in Indonesian firms, the influence of insiders, state enterprises, and foreign ownership on dividend policy in manufacturing companies in Indonesia was analysed in this study. Large majority shareholder may influence the decision on firm dividend policy. Using their power, large shareholder may adopt dividend policy that reduce the private benefit consumed by management, yet they can also enforce misappropriate firm's cash flows at the expense of minority shareholders through distribution profit. Mulyani et al. (2016) found that the family as dominated owner pay less dividend in Indonesia, it seemed that there was expropriate cash flow from the company. Insiders, state ownership and foreigners are also appear as the larger proportion ownership in Indonesia. When majority owner is insider, they tend to distribute lower dividend and tunnelling the firm cash flow through accumulating retained earnings (Truong & Heaney, 2007). Firm with higher government ownership is most likely to pay higher dividend in the country with weak protection of minority shareholder, returning the cash flow to the government is dominant than convey the signal to the market (Lin et al., 2017). Meanwhile, the foreigners that have majority ownership in the firm may reduce the dividend payment, this indicates that foreigners have good corporate governance and do not disgorge cash from the firm (Lam et al., 2012). Thus, the existence of the majority shareholder and the relationship with the dividend payout in

the Indonesian company is still interesting to be reviewed to get a better understanding of the dividend policy

In accordance with the signaling theory of Ross (1977) and De Angelo et al. (2004), the results showed that the greater a firm's profits, the higher its profit distribution or dividend payment to shareholders. Government-controlled companies tended to share higher profits with owners, but the dominance of foreign ownership led to a decrease in the dividend payout. Foreign companies tended to cut the dividend payment and guided the profit flow back to the firm. However, these companies may face difficulty-obtaining approval from principals abroad to increase capital in foreign direct investment schemes. Additionally, the association between the insiders as majority owner in the company is negative, but not significant. Thus, it cannot be proven that insiders are engaged in cash disgorging.

The remainder of this paper is structured as follows: the second part describes the literature reviews that are used in this research; the third section discussed data collection methods and research methodologies; the fourth section includes descriptive statistics and analysis of research results; lastly, the fifth section concludes this study and presents the implications.

Literature Review

Profitability and Dividend Payment Policy. Dividends as a distribution of profit to shareholders can be used as a signal to outside parties to indicate that the

company's financial condition is healthy enough (DeAngelo et al., 2004; Ross, 1977). In other words, the company does not require financing either from internal or external sources in order to invest in other projects in the future (Vasigh et al., 2010).

Fama and French (2002) through the pecking order model and trade off theory confirmed that the higher a firm's profits, the higher the dividend payout was distributed to shareholders. Empirical findings from several countries prove that when firms earn higher profits, they have a tendency to distribute large profits as well. This conveys a signal to the market that the company is in a healthy financial position and expects an increase in stock prices in the market, as signaling theory suggests (DeAngelo et al., 2004; Ross, 1977). The most recent empirical study supports this theory was by Hwang et al. (2013), for example, who showed consistently that the firms' profit positively impacted the dividend payout of the chaebol conglomerate in South Korea. Firth et al. (2016) and Huang et al. (2011) also indicated that the firm's profitability was still the main factor determining dividends payment in China. The same results were obtained by Jabbouri (2016) in Middle East and North Africa (MENA) countries, and Mulyani et al. (2016) in the Indonesian market.

Ownership Structure and Dividend Payment Policy. Agency theory, initiated by Jensen and Meckling (1976), suggested that a conflict of interest between the management and the owner of the company may alter the firm's stability to please both

parties. Dividend payout is one of the corporate governance mechanisms that can alleviate conflict. This distribution of profits, as described by Jensen (1986), can reduce the company's free cash flow that managers can use for unprofitable projects or for benefiting themselves unwisely. Additionally, Easterbrook (1984) stated that the reduction of free cash flow through dividend payments forced managers to seek external funding so that it could improve the discipline of managers due to the limitations and controls imposed by the creditors. Majority ownership, according to alignment effect theory, as stated by Easterbrook (1984), may provide better monitoring due to the better alignment between majority shareholders and managers. Consequently, this leads to effective policy in dividend payment. Meanwhile, under the entrenchment effect, majority owners have significant power to misappropriate the firm cash flows at the expense of minority shareholders, which leads to inefficient dividend policy.

Furthermore, the strength of management discretions in dividend policy may be caused by the fact that those managers are appointed by majority shareholders, concentrated by groups such as families, institutions, or insiders. These owners have significant power and control over decision-making that must be followed by managers (La Porta et al., 2000). Managers use their discretion to pay out dividends that benefit the majority shareholders. Using power and control, they dredge cash from the company and then distribute small dividends

to minority shareholders. La Porta et al. (2000) and La Porta et al. (1999) suggested that ownership of public listed companies was still concentrated within limited parties. Therefore, it is not unusual for the majority shareholder to control the management position in the company. Furthermore, La Porta et al. (2000) developed two dividend policy models. The first model is the outcome model, which states that firms pay higher dividends because of the pressure from the minority shareholders and improvement of corporate governance. Meanwhile, the substitute model emphasizes that the company must maintain its good reputation by paying dividends as a substitute control mechanism. The dividends are used to attract external investors in the capital market, and thus, the insiders are expected to pay higher dividends and reduce the firm's cash flows that could be left for expropriation.

Faccio et al. (2001) studied the impact of corporate governance on dividend payout in an international setting. They showed that dominance shareholders used the dividend payment as a scheme to disgorge firms' cash flows from minority investors. These authors also provided evidence that when group businesses or institutions had large control over a company, they paid higher dividends in European zones than in Asia. Additionally, these authors suggested that expropriated cash from minority shareholders through dividend policy was diminishing in European countries, while this problem was worsening in Asia.

A recent study by Gonzalez et al. (2016) involved companies in several Latin

American countries revealed a negative relationship between the concentration of ownership and dividend payout. This occurred especially when the largest investor in the company was an individual. The authors identified a cash expulsion from the company at the expense of the minority shareholder. Furthermore, if the firm is located in a country that adopts a common law legal system, dividend payouts tend to be higher. Meanwhile, companies that cross-list their stocks in the international market and control them through insiders as majority investors tend to pay higher dividends, in accordance with the signaling hypothesis (Esqueda, 2016). Truong and Heaney (2007) also examined the impact of the majority of shareholders and the policy on dividend policy across countries. They recorded a negative relationship between shareholder concentration and dividend payout policy. When the majority of shareholders were insiders or financial institutions, then dividend payouts tended to be smaller.

Some extant studies focus on the impact of concentration ownership and dividend policy in one country, such as Hwang (2013) in Korea, Mulyani et al. (2016) in Indonesia, and in the United Kingdom (UK) by Khan (2006). Hwang et al. (2013) analyzed the corporate governance behavior of dividend payments by business groups (chaebol). Authors showed that these business groups had good corporate governance; however, they were weak in shareholder protection and paid lower dividend payout compared to the non-group business companies.

Additionally, the authors conclude that dividend payments could not be used as a control mechanism in corporate governance in Korea, especially for chaebol.

Empirical tests conducted by Mulyani et al. (2016) noted that family-dominated companies paid fewer dividends in public listed companies in Indonesia. Families' owners tended to use their power to dredge cash from the minority shareholder; this finding is in accordance with Esterbrook (1984). The role of dividends as control mechanisms has not been used to minimize the problem of agency within the company dominated by families in Indonesia. These results arise probably due to the weak protection for minority shareholders from the government and weak law enforcement. In contrast to Mulyani et al. (2016), family-controlled firms pay higher dividends in the European zone (Pindado et al., 2012). The dividend payout policy has been effectively implemented to monitor corporate management because of aligned interests between majority shareholders and managers.

Several studies investigate the impact of majority ownership by institutions, foreign ownership, and state enterprises' ownership on dividend payments. A study in China by Firth et al. (2016) suggested that a mutual fund as the majority owner institution distributed larger dividends, however other financial institutions had no effect on the decision to pay cash dividends. This result is more pronounced if mutual fund owners are controlled by the government and have strong cash flows. When the company is

dominantly owned by foreigners in China and cross-lists its stocks, it tends not to pay dividends (Lam et al., 2012). The higher the proportion of foreign ownership, the smaller the dividend payments are; this conveys a signal to the market that foreigners do not expropriate cash from the firms and have good corporate governance. The difficulty of obtaining additional capital from principals abroad may force such companies to use internal financing, thereby lowering the distribution of profit.

Majority shareholders have better corporate information than minority shareholders, thus there is a positive relationship between ownership concentration and asymmetric information. The concentration of ownership affects the transmission of information to other parties. Insiders tend to restrict disclosure information, resulting in problems in corporate transparency. Lin et al. (2017) proved that companies in China Taipei with asymmetric information between majority and minority shareholders tended to pay lower dividends. However, state-owned enterprises with very high asymmetric information pay higher dividends than private companies. This is due to the weak protection of minority investors and the weak institutional environment in the country. Meanwhile, Gugler (2003) showed that government-controlled companies tended to smooth their dividend payouts.

MATERIALS AND METHODS

Data

This study used financial data from 2009

to 2015 regarding public listed companies from the manufacturing industry sector that were actively traded in the stock market. There were 42 companies in this sector that provided financial reporting from the time periods under examination. However, only 34 firms were included under the data criteria. Those companies must be actively traded and pay dividends each year during the study period. The financial data of the companies were taken from either the financial statements of each of the company's website or from the Indonesian stock exchange website (www.idx.co.id) and iCAMEL. The explanation of ownership data was obtained through the annual report and additional information contained in the financial statements along with public news/publication.

Variable Definition

Table 1 presented below is a summary of the variables used in this study, along with the definition. The main variables in this study were dividend ratio (Faccio et al., 2001; La Porta et al. 2000, Mulyani et al., 2016), profitability (DeAngelo et al., 2004; Truong & Heaney, 2007), ownership by insiders (Esqueda, 2016; Truong & Heaney, 2007), ownership by state enterprises (Gugler, 2003; Lin et al., 2017), and ownership by foreigners (Gugler, 2003). The ownership variable was calculated simply by calculating the proportion of the number of stocks owned by the owner (insiders, state enterprises, or foreigners) over the total number or value of the company's stock. Some control variables

were also included in this study which were current ratio, debt to equity ratio, size of firm, company growth rate, and economic condition. These control variables were measured by the growth rate of the capital market and were expected to be associated with dividend payout in accordance with the previous findings.

Table 1

Variable definition

Variables	Definition	Reference	Predicted sign
Dividend Payout Ratio (DPR)	Dividend Payout Ratio (DPR) is measured by comparing the amount of dividend per share with earnings per share. Thus the formula is the firm's dividend per share divided by earnings per share.	La Porta et al. (2000), Mulyani et al. (2016)	NA
Profitability	Measured using ROA, net profits over total assets. Alternatively, measuring using Net Profit Margin, net profit divided by total sales	DeAngelo et al. (2004), Jabbouri (2016), Mulyani et al. (2016)	+
Managerial ownership	% of shares held by insiders (managers, directors, executives) over firm's total capital/shares	Esqueda (2016), Truong and Heaney (2007)	-
State ownership	% of shares held by government entities over firm's total capital/shares.	Gugler (2003), Lin et al. (2017)	+
Foreign ownership	% of shares owned by foreigner investors over firm's total capital/shares.	Firth et al. (2016), Lam et al. (2012)	+/-
Liquidity	Current Ratio (CR) represents the comparison between firms' current asset and current liability. To measure CR, simply divide current asset with current liability.	DeAngelo et al. (2004), Jensen (1986), Jabbouri (2016)	+
Leverage	Debt-to-Equity measures how big an enterprise is financed by debt rather than with equity capital. Thus, Debt-to-Equity Ratio (DER) is measured by dividing total liabilities by total shareholder's equity.	Gonzalez et al. (2016), Jensen, Meckling (1976), Mulyani et al. (2016)	+/-

Table 1 (Continued)

Size	The natural logarithm of the total asset.	Gonzalez et al. (2016), Esqueda, (2016), Mulyani et al. (2016)	+
Growth	Asset growth is measured by dividing the subtracted result of current year total asset and previous total asset with previous year total asset.	Jabbouri (2016), La Porta et al. (2000)	+/-
State of the economy	The yearly return of the market main index (Market Return/IHSG)	Jabbouri (2016)	+/-

Research Model

This study uses a panel data regression model and the empirical model is written as follows:

$$DPR_{it} = \alpha + \beta_1 ROA_{it} + \beta_2 NPM_{it} + \beta_3 INSD_{it} + \beta_4 STATE_{it} + \beta_5 FORG_{it} + \beta_6 CR_{it} + \beta_7 DER_{it} + \beta_8 GROWTH_{it} + \beta_9 SIZE_{it} + \beta_{10} MR_{it} + \varepsilon_{it} \dots (1)$$

- Where,
- DPR : Dividend payout ratio
 - ROA : Return on asset
 - NPM : Net profit margin
 - INSD : P r o p o r t i o n ownership by insiders
 - STATE : P r o p o r t i o n ownership by state-owned enterprises
 - FORG : P r o p o r t i o n ownership by foreigner
 - CR : Current ratio
 - DER : Debt to equity ratio
 - GROWTH : Growth of firm's assets
 - SIZE : Size of firm's assets, using ln Asset
 - MR : Capital market return represented of economic growth

RESULTS AND DISCUSSIONS

Descriptive Statistic

Table 2 reveals that the average dividend payout ratio in manufacturing companies in Indonesia was relatively low at only 25.79% of the profit, although some companies distributed dividends higher than profit margin earned in the same year. The return on assets was at 10.66%. Meanwhile, the proportion of ownership data showed that the average proportion of insiders' ownership was only about 3.56%, while the average share of ownership by state enterprises was much smaller that was 1.53%. The proportion of foreign ownership was much higher at 41.74%.

Result Analysis

Table 3 lists the results of the static panel data regression using the fixed effect model. Time effect was included in data processing to capture the year-specific effect, meanwhile firm-fixed effect was used to analyze, for example, how different types of ownership or size influence the dividend payout.

Table 2

Descriptive statistics

	Mean	Median	Max	Min.	Std. Dev
DPR	0.2579	0.1770	1.3816	-0.6047	0.3105
ROA	0.1066	0.0835	0.6691	-0.0385	0.1006
NPM	0.1058	0.087	0.5178	-0.0548	0.0896
INSD	0.0356	0.000	0.2888	0.0000	0.0802
STATE	0.0153	0.000	0.2630	0.0000	0.0536
FORG	0.4174	0.5005	0.9631	0.0000	0.2758
CR	2.8442	2.0300	13.6500	0.4800	2.4015
DER	1.0597	0.7300	10.1600	0.0900	1.3310
GROWTH	0.1507	0.1179	0.8543	-0.3235	0.1721
SIZE	1.40E+13	2.16E+12	2.45E+14	7.28E+10	3.85E+13
MR	0.2081	0.1046	0.7640	-0.0448	0.2711

Table 3

Regression results, DPR is the dependent variable

	1	2	3
Constant	2.114 * (0.082)	2.733 ** (0.026)	1.912 (0.118)
ROA	1.071 *** (0.003)		1.559 *** (0.003)
NPM		0.504 (0.171)	-0.668 (0.210)
INSD	-1.713 (0.109)	-1.649 (0.134)	-1.789 * (0.095)
STATE	27.781 *** (0.001)	24.165 *** (0.005)	28.700 *** (0.000)
FORG	-0.304 (0.185)	-0.325 (0.168)	-3.029 (0.187)
CR	0.032 * (0.055)	0.035 ** (0.049)	3.673 ** (0.034)

Table 3 (Continued)

DER	0.031 (0.102)	0.025 (0.222)	3.492 * (0.085)
GROWTH	-0.127 (0.332)	-0.054 (0.684)	-0.109 (0.403)
SIZE	-0.079 * (0.061)	-0.097 ** (0.024)	-0.073* (0.088)
MR	-0.274 *** (0.002)	-0.272 *** (0.003)	-0.268 *** (0.002)
R square	0.568	0.546	0.574

The first and second column separates profitability variables. In the first column, the variable used is Return on Assets (ROA), while the second column used Net Profit Margin (NPM). These two variables are separated because of the relatively high correlation coefficient rates between the two and hence could cause a multi-collinearity problem. Both results are run with the same level of year between dividend payments and explanatory variables. Following Firth et al. (2016) and Kang et al. (2016), this study also investigated the effect of the lag one-year value of explanatory variables on future dividend payment on column three. These authors explained that some endogenous nature variables such as ownership and other variables did not easily produce conclusive evidence on its relationship with dividends. Thus, to solve this problem partially, the lag of one-year independent variables was regressed and the results are shown in column 3 (three).

Regression results indicated that profitability was one of the factors that

must be considered in dividend payment policy. ROA is positively and significantly in association with dividends. The higher the company profit, the greater the dividends that are available to distribute to shareholders. These findings are consistent with the results of Fama and French (2002), Truong and Heaney (2007), as well as the hypotheses signaling theory by Ross (1977). The company conveys good prospects for financial signals to the market. However, the alternative measurement profitability, namely net profit margin (NPM), does not significantly affect dividends.

The proportion of ownership variable showed a negative relationship between insider ownership and dividend payout, however this association is not significant. Thus, it is insufficient to prove that the exploitation of a firm's cash flow by insiders occurs at the expense of the minority shareholders in manufacturing companies in Indonesia. Cash expropriation by the majority shareholder was obtained by Truong and Heaney (2007). In contrast,

Esqueda (2016) proved that dividend payouts by insider-controlled firms were higher in companies that cross-listed their shares in some markets, as suggested by the signaling theory.

Firms that have a larger proportion of state-owned enterprises tend to pay higher dividends, as evidenced by the positive relationship between STATE and dividend payout variables. The coefficient of this variable is relatively high which indicates that the government influences the decision to pay higher dividends. This phenomenon emerges because the government needs more funds from state enterprises to finance the state budget. Political consideration could be one consideration, as managers from political parties appointed by the government would convey the message to the market that they have managed the firm properly and thus pay higher dividends (Gugler, 2003). Another explanation is that the government reduces the availability of cash flows for managers, so that it is not used for managers' personal benefit, or because of the asymmetry information between majority shareholders and minorities, such as in the case of Taiwan (Lin et al., 2017).

The foreign ownership variable indicates a negative relationship. This negative relationship indicates the possibility that these foreign firms cut dividends as they put most of the profits back into capital. This may happen because of the difficulty to get approval from principals abroad to increase capital in foreign direct investment schemes.

Furthermore, the control variable, liquidity, had a positive and significant

sign, and leverage had a positive relation and is also significant. The liquidity ratio as measured by CR (current ratio) showed a positive relationship result on dividend payout. A liquid company seems to have higher availability of current assets, which can be converted into cash easily to pay higher dividends. Debt and capital ratio variable (DER) exhibited a positive link with dividends, but with a very weak level of significance. These positive signs provided an indication that the higher the leverage (DER) the greater the company's dividend payments made by the company. This is in contrast to the theory presented by Jensen (1986), who stated that leverage could be used as a corporate control mechanism. External funding sources are part of the corporate governance, whereby with increasing debt, it will allow strict control of creditors to the company's cash flow. These differing results might occur due to a lack of supervision from the creditor to the company in the case of dividend payout decisions. Other possibilities are the strong power of majority shareholders and low-level protection of shareholders' rights and creditors (La Porta et al., 2000).

Other control variables such as growth or asset growth, firm size, and market growth all demonstrated a negative sign relationship. Increased asset growth and asset size required relatively large funding for operational and investment, so funds internally generated by firms needed to flow back to the company. This led to lower dividend payouts. This result is in line with the findings of previous studies such as

Faccio et al. (2001), Gonzalez et al. (2016) and Hwang et al. (2013).

Furthermore, economic growth, which proxies for the growth rate of the market index, showed a negative relationship with dividend payout policy. This finding is in line with Jabbouri's (2016) study in the MENA market. This relationship might arise because in the economic expansion, investors are more concerned with capital gains, so they might have less focus on the payment of dividends. This fact also supports the findings obtained by Mitton, 2002, Rajan and Zingales (1998), Shleifer and Vishny (1997), as in a booming market period, good corporate governance mechanisms are not the main focus of regulators and investors, so the dividend payout is not a concern of investors.

CONCLUSIONS

This study aims to reevaluate the effect of firms' profitability on dividend policy. It further reexamines the effect of the large proportion of company ownership by insiders, state enterprises, and foreigners on dividend payout policies. Dividend payment is a control mechanism used in corporate governance to alleviate conflict between shareholders and managements (Jensen, 1986; Jensen & Meckling, 1976). Payment of dividends results in the reduced availability of cash flows in the company, which can be applied to reduce management discretion for unfavorable investments or for personal benefits (Easterbrook, 1984). Furthermore, the concentration of company ownership in certain groups has an impact

on the higher discretion on the dividend payout policy. Managers appointed by majority shareholders make decisions on dividend payout, which benefits the majority shareholders. Without sufficient controls, majority shareholders expropriate firms' cash flows and distribute lower dividends to minority shareholders (La Porta, 1999, 2000). The findings reveal that an increase in profitability affects dividend payout positively; this is in line with the signaling theory by Ross (1977). This finding conveys a good signal to investors on the prospect of a company's financial condition (Benavides et al., 2016; DeAngelo et al., 2004; Fama & French, 2002; Truong & Heaney, 2007). An increase in the proportion of ownership by insiders consistently has a negative relationship with dividends, but it is not significant. There is probably early indication of exploitation of the company's cash flows at the cost of minority shareholders in the Indonesian capital market and to prove this, more samples are needed in the research. Meanwhile, the higher the government's ownership of the firm, the higher the dividend payout would be. Political elements and the profit contribution of state enterprises for government expenditures and high information asymmetries are important factors in the dividend policies among companies with high concentrations of ownership by state enterprises (Gugler, 2003, Lin et al., 2017). Ownership by foreigners shows a negative relationship with dividend payout. The difficulty of obtaining additional capital from foreign principals may be the cause of reduced

dividend payouts, while the foreigners rely more on internal funding sources. Another possibility, in line with Lam et al. (2012), is that foreigners investing in Indonesia do not dredge the firm's cash flow.

These results provide implications regarding policy makers, regulators, and investors who invest in the Indonesian capital market. Policy makers should pay attention to the existence of cash flow extraction symptoms by majority shareholders, especially in companies that are controlled by insiders. It leads to losses on minority shareholders. To mitigate this problem, firms need to enhance the transparency of corporate management in financing, improvement of corporate governance, and increased protection in shareholder rights. Financial Authority Services should also apply strict supervision of a firm's corporate governance that results in the loss of minority investors. Investors who expect to have incremental dividend payments regularly should consider the owners of the company. Government-controlled firms are the more appropriate option for this type of investor.

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