Relevance of Free Cash Flow, Profitsability, Liquidity, Leverage, Firm Size, and Price Earnings Ratio to Dividend Policy

Bayu Wijayantini[1], Mohamad Rivaldi Darmawan[2], Alfi Arif[3]
bayu@unmuhjember.ac.id [1], mohammadrivaldid@gmail.com [2], alfi.rif@unej.ac.id [3]

Muhammadiyah Jember University, Jember University

Abstract. Changes in the size of dividends are used as a benchmark for good or bad from the company's ability to run its business in the future. The purpose of this study is to analyze the effect of free cash flow (FCF), return on equity (ROE), current ratio (CR), debt to equity ratio (DER), firm size (SIZE) and price earning ratio (PER) on dividend payout ratio (DPR) at HIMBARA member banks for the 2015-2021 period. This study uses 60 observational data from 4 companies, namely BBRI, BBNI, BBTN and BMRI. From the results of data processing, it can be concluded that free cash flow (FCF), return on equity (ROE), current ratio (CR), debt to equity ratio (DER), firm size (SIZE) and price earning ratio (PER) have a positive effect on dividend payout ratio (DPR).

Keywords: free cash flow, return on equity, current ratio, debt to equity ratio, firm size, price earning ratio, dividend payout ratio.

1 Introduction

Investing is one of the many fund decisions that a company manages to generate future profits [1]. Investing in businesses, especially long-term businesses, can be affected by many factors, the most important of which is the availability of funds. One of the main factors affecting the availability of funds is the achievement of profit or profitability. Investors prefer dividends to capital gains because they are more certain than uncertain capital gains. Therefore, the main factor that management considers when determining the amount of dividends is the security aspect that generates cash flow, and tends to provide higher dividends year by year [2].

Dividend policy is one of the main tasks of the company's finance manager. It is important to note that this policy is directly related to the company and the shareholders (investors). In the case of a company, paying dividends reduces the amount of funds returned to the company in the form of retained earnings. For shareholders, dividends are the income that affects their wealth. Surveys on the determinants of a company's dividend payment ratio are widespread in various countries, both Asia and Europe. Existing research shows that there are many factors that have a lasting impact on dividend policy. For example, the liquidity of a company, its ability to generate profits (profitability), its ability to pay short-term debt (liquidity), and the size of the company. Dewasiri et al. Summarizing the results of a survey of capital markets in developing and developed countries, he discovered many factors that influence dividends and the company's dividend policy [3].

Dividend policy determinants have been studied for decades, but it is uncertain which factors will affect dividend payments. Surveys have been conducted using variables such as dividend payment rate (DPR) and other determinants of dividend policy, but the results are often inconsistent. For example, in 2016, Sarmento identified profitability and liquidity as positive determinants affecting dividend payment rates in 16 emerging markets [4]. Meanwhile, Narayanti argues that profitability is a negative determinant and liquidity, the current debt indicator, is a negative determinant, similar to the DPR indicators of companies registered in Turkey [5]. The dividend payment ratio of HIMBARA member banks listed on the Indonesia Stock Exchange (IDX) varies greatly from bank to bank during the period from 2017 to 2021. All of these indicators are listed in the following table [6].

Table 1. List of Dividend Payout Ratio of HIMBARA member banks listed on the BEI period 2017 -2021

		Dividend Payout Ratio **(%)**				
No	**Company**	**2017**	**2018**	**2019**	**2020**	**2021**
1.	PT Bank BRI Tbk	25,08%	29,81%	18,67%	40,03%	47,80%
2.	PT Bank BNI Tbk	25,09%	20,75%	28,11%	20,75%	25,09%
3.	PT Bank BTN Tbk	22,31%	14,97%	17,97%	21,74%	26,88%
4.	PTBank MANDIRI Tbk	23,42%	41,11%	57,44%	35,12%	39,04%

Source : www.idx.co.id

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From the table above, we can see that the dividend rates of each HIMBARA member bank are the same, not different, and not even. So there must be a specific reason for the difference. Causes include lower cash flows, lower profits, higher corporate bonds, and lower liquidity, which affect the value of dividend payments, which tend to fluctuate. The bank itself is a very important institution in maintaining the financial stability of the country. Banking functions must carry out their activities according to the principle of prudence (prudential banking). It is based on the characteristics of a prudent bank, that is, a bank that is always careful not to endanger its customers or the country's economy when doing business. In the event of a currency crisis at any point, the banking system can survive by maintaining domestic financial stability. As it is today, more specifically, from mid-March 2020, Indonesia's banking sector has undergone various types of testing as Indonesia faced a Covid-19 pandemic crisis. Various business industries such as state-owned banks and HIMBARA were also affected. Various stimulus measures have been implemented to stabilize the country's economy, one of which is the stimulus measure implemented by the Indonesian government, the National Economic Recovery (PEN).

On June 25, 2020, the State Bank (HIMBARA) received a deposit of IDR 30 trillion from state funds. Each received a deposit of IDR 10 trillion at Bank Mandiri, IDR 10 trillion at Bank BRI, and IDR 5 trillion each at Bank BNI and Bank BTN. Four months later, on September 30, 2020, Treasury Minister Sri Muryani Indrawati again added HIMBARA's government funding. In this second phase, 17.5 trillion rupiah was added, Bank Mandiri, BRI and BTN each received 5 trillion rupiah, and BNI Bank invested 2.5 trillion rupiah. Therefore, the total amount of funds invested in HIMBARA is currently 47.5 trillion rupiah (CNBC, Indonesia).

2 Literature Review and Hypotheses Development

Dividend policy serves as a source of information about a company's public financial performance. Financial performance consists of market performance related to stock prices. One of the investors' motives for stock prices is capital gains or dividends. Dividends are generated from profit sharing and later distributed to investors in the form of stock or cash dividends. In other words, paying dividends is a positive sign that the company is basically doing well. Dividend payments serve as a source of information and reflect the investor's assessment of corporate profits. If it is not paid, investors tend to think that the company's financial performance is struggling. Changes in dividend levels reflect the company's ability to generate future profits[7]

Financial indicators used to determine the direction of future dividend policies include free cash flow (FCF), profitability (ROE), liquidity (CR), leverage (DER), company size (SIZE), and Includes price-earnings ratio (PER).). There are some previous survey data that have different perceptions of the factors that influence a company's dividend policy. Some mention the relevant results between the levels of net cash flow, profitability, liquidity, debt ratio, company size, and price-earnings ratio. These have a positive impact on a company's dividend policy and vice versa. However, some other researchers have found that the company's dividend policy is not only the company's free cash flow level, profitability, liquidity, leverage, company size, and price-to-revenue ratio, but also the company's dividend. The company's environmental conditions and the country's global economic and environmental conditions are also affected by the level of the company. Yet another factor. High payout rates do affect investor confidence, and the public can even attract investors [8]. As a result, many researchers have different views on what factors affect a company's dividend policy.

Profitability, liquidity (cash ratio), leverage and company size have a significant positive impact on dividend policy [9]. Pradnyavita and Suryanawa found the same thing. In short, free cash flow and profitability have a positive impact on dividend policy [10], and Cahyani also shows a significant relationship between reported net cash and cash dividends at the end of the year [11]. Meanwhile, Nurfatma and Purwohandoko stated that free cash flow, profitability, liquidity, debt and company size did not affect dividend policy [12]. Pradana and Sanjaya also state that free cash flow does not affect dividend payments [13]. Dirman et al. also states that the debt-to-capital ratio and price-earnings ratio do not affect dividend payments [14].

3 Research Method

The population used in this survey is HIMBARA member banks listed on the Indonesia Stock Exchange from 2015 to 2021. HIMBARA's member banks consist of PT Bank BRI Tbk, PT Bank BNI Tbk, PT Bank BTN Tbk, and PT Bank MANDIRI Tbk. In addition, the five-year data was collected in a different way than the annual financial statements of the four HIMBARA members. Bank. The extracted data is in the form of financial reports from various sources, including the first data from the Indonesia Stock Exchange (IDX) published at www.idx.co.id. In addition, the second is from www.eddyelly.com and the third is from the accounting profile of each company that issues an annual or financial report each year (annual report) [6].

This study uses quantitative analysis techniques and regression procedures. To test the hypothesis, perform multiple linear regressions (many independent variables) using a panel data model or a method of combined data from many objects (sections) and time series (time series). To prove the correctness of the proposed hypothesis, this study temporarily uses one of the methods for estimating regression models, or an approach that is a panel data model, the common effects model. The rationale for this study using the estimation model approach is to combine only time series and cross-section data.

In addition, the correct panel data regression model estimation (Chow test) is selected. The reason for this test is to determine the best model between the fixed effects model and the common effects model. If the result accepts the null hypothesis (probability> 0.05), then the best model to use is the common effects model. However, if the results show that the null hypothesis (probability <0.05) is rejected, then the best model used is the fixed effects model. Further tests are performed, followed by (Houseman test) and (Lagrange multiplier test).

In this study to estimate the panel data model by using the panel data regression equation formulation as follows.

$$DPR = \alpha + b_1 FCF_{1it} + b_2 ROE_{2it} + b_3 CR_{3it} + b_4 DER_{4it} + b_5 SIZE_{5it} + b_6 PER_{6it} + e$$

Which:

Dividend Payout Ratio (Y)	=	Dependent Variable
α	=	Constanta
Free Cash Flow (X_1)	=	Independent Variable 1
Return On Equity (X_2)	=	Independent Variable 2
b (1,2…)	=	Coefisien
e	=	Error
t	=	Time
I	=	Bank HIMBARA

4 Result and Discussion

From the 84 data processed, namely FCF, ROE, CR, DER, SIZE and PER of HIMBARA member banks, the following results were obtained.

Table 2. Partial Test Result

Variabel	Prediksi	Coefficient	Std. Error	t-Statistic	Probabilitas	Summary
FCF	Positif	0,2767	0,1112	2,4878	0,0179	Signifikan
ROE	Positif	0,1707	0,2419	0,7057	0,4851	Not Signifikan
CR	Positif	0,4917	0,1097	4,4808	0,0001	Signifikan
DER	Positif	0,0602	0,0836	0,7202	0,4763	Not Signifikan
SIZE	Negatif	-0,1390	0,1332	-1,0433	0,3041	Not Signifikan
PER	Positif	0,7266	0,1255	5,7853	0,0000	Signifikan
C		-8,4525	3,8827	-2,1769	0,0365	
Cross-section fixed (dummy variables)						
Fixed Effects (Cross)						
BBRI--C		-0,1350				
BBNI--C		-0,6672				
BBTN--C		0,2445				
BMRI--C		0,5577				
R-squared : 0,9592 Adjusted R-squared : 0,9484						
F-statistic		8,9347				
Prob(F-statistic)		0,0000				

Source : data processed

Free Cash Flow, Current Ratio and Price Earning ratio has a significant positive effect on the Dividend Payout Ratio at HIMBARA member banks. Return On Equity and Debt Equity Ratio have a positive and insignificant effect on the Dividend Payout Ratio at HIMBARA member banks. But, firm size has an insignificant negative effect on the Dividend Payout Ratio at HIMBARA member banks

It can be concluded that free cash flow (FCF), net income (ROE), short-term debt (CR), debt equity (DER), total assets (SIZE) and share prices (PER) at HIMBARA member banks can affect dividend distribution. to shareholders. This is in accordance with several theoretical points of view, one of which is that the increase in the free cash flow indicator will have a positive impact on increasing dividends which will then be distributed to shareholders. This is in accordance with previous research, namely Pradnyavita and Suryanawa which states that the free cash flow ratio has a significant positive effect on dividend payments[13]. Cahyani's research also states that cash flow has a positive effect on the Dividend Payout Ratio [11]. However, on the contrary, the results of this study contradict the research of Nurfatma and Purwohandoko which states that free cash flow has no effect on dividend policy[12]. Meanwhile, Pradana and Sanjaya state the same thing that free cash flow has no effect on dividend payments[13].

Thus it can be concluded that the condition of cash (free cash flow) has a varied role in determining the direction of dividend policy. The next theory states that an increase in the company's Return On Equity is expected to be able to attract investors to invest a number of their funds[14]. This is in accordance with previous research, namely Saadiah and Wahono which revealed that there was a significant effect of profitability on dividend policy[15]. Dirman et al. also reveals the same thing that profitability has an effect on dividend distribution[16]. Thus, it can be concluded that profitability (net income) has a positive role in determining the direction of dividend policy. In contrast, Nurfatma and Purwohandoko state that profitability has a negative effect on dividend policy[12].

Another theory states that the Current Ratio (current debt) itself is used to determine how well the company's ability to meet short-term obligations. This means that the better the cash position and liquidity position of the company, the better the ability to pay dividends. This is in accordance with previous research, namely Saadiah and Wahono stating a significant positive effect of liquidity on dividend policy[15]. In contrast, research by Nurfatma and Purwohandoko states that liquidity has no effect on dividend policy[12]. Thus it can be concluded that liquidity (current debt) has a varied role in determining the direction of dividend policy.

5 Conclusion

Based on the results of hypothesis testing, it has been proven that there is a varying effect between the independent variables on the dependent variable. Free Cash Flow, Current Ratio and Price Earning ratio has a significant positive effect on the Dividend Payout Ratio at HIMBARA member banks. Return On Equity and Debt Equity Ratio have a positive and insignificant effect on the Dividend Payout Ratio at HIMBARA member banks. But firm size has an insignificant negative effect on the Dividend Payout Ratio at HIMBARA member banks. Based on the theory that has been put forward in the theory review, there is one theory that relates to the condition of the free cash flow variable, namely signaling theory. The reason is that this theory reveals that the dividend cash paid is considered by investors as a signal of the company's prospects in the future. This means that the better the level of cash flow of HIMBARA banks, the better the level of dividend cash paid to investors. Basically free cash flow (cash condition) is used as capital expenditures (CAPEX) so that cash has a function to support operational activities and as a determinant of the direction of dividend policy in the future. The higher the Return On Equity owned, it will increase the amount of Dividend Payout Ratio. Basically profitability (net income) is generated from the company's operational activities and then used as a determinant of the direction of dividend policy in the future. As for the better the Current Ratio, it will increase the amount of Dividend Payout Ratio. This means that liquidity (current debt) is one of the obligations that must be paid at maturity which is short-term, which is less than one year and is then used as an indicator to determine the direction of dividend policy in the future. In contrast to the Debt To Equity Ratio, if this indicator increases, it will reduce the amount of dividends. Basically, leverage (fixed debt) is a debt management activity that functions as a support for long-term operational activities, which is above one year and is used to maximize profits and is then used as an indicator to determine policy direction. Furthermore, the Firm Size ratio, if this ratio increases, it will increase the amount of dividends. Basically, firm size is generated from the total assets (assets) owned in a certain period which includes current assets and fixed assets and is then used as an indicator to determine the direction of dividend policy in the future. The last ratio is the Price Earning Ratio, if this ratio increases, the dividend value will also increase. Basically the price earning ratio (stock price) is used as investment management management (equity) and then used as an indicator to determine the direction of dividend policy in the future. All existing financial ratios need to be considered if HIMBARA member banks want the dividend payout ratio value to be stable and prudent. One of them is that HIMBARA member banks must maintain the FCF, ROE, CR, DER, SIZE and PER values because these variables have a direct impact on the movement of the dividend payout ratio and make it attractive for investors.

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