The Effect of Corporate Governance on Dividend Policy and Firm Size as Moderating in Jakarta Islamic Index

Muhamad Farizd Fajdy[1], Muhamad Umar Mai[2]
{muhammad.farizd.kps19@polban.ac.id[1]}

Politeknik Negeri Bandung, Indonesia[1, 2]

Abstract. A firm exists because it has the purpose that is to maximize the investors' welfare and dividend payments are one of the ways that companies do to achieve this purpose. The consistency and size of the dividend payout ratio is a crucial thing to be considered by the company's management because it is one of the determining factors for investors in investing their funds in the company. The objective of this study was to determine the moderation of firm size on the effect of corporate governance on dividend policy. Corporate governance is proxied by the size of the Board of Directors, Institutional Ownership, and Independent Board of Commissioners variables. The population in this study is all companies listed at Jakarta Islamic Index (JII) from 2010-2019. The sample is determined using a purposive sampling technique with the criteria of companies paying dividends. The method of data analysis in this study used the Partial Least Squares – Structural Equation Modeling (PLS-SEM). The results found that firm size moderated negatively on the effect of the Independent Board of Commissioners on the Dividend Payout Ratio. Furthermore, the results showed that Institutional Ownership directly had a positive effect on the Dividend Payout Ratio. While the Independent Board of Commissioners had a direct negative effect on the Dividend Payout Ratio.

Keywords: Dividend Payout Ratio, Institutional Ownership, Board of Directors, Independent Board of Commissioners, Firm Size

1 Introduction

Today's capital market has played a very fundamental role in the economy of a country by carrying out its intermediation capacity which provides opportunities for companies to increase funding from investors. However, this very large role is not accompanied by good investor growth. The number of investors in the capital market reaches 363,000 people, but this number is relatively small compared to the ratio of the number of Indonesian people who touch more than 240 million, so it can be concluded that the growth is not optimal [1]. This indicates that investors are still less interested in investing in the capital market because one of them is inconsistent dividend payment policies [2].

The consistency of dividend distribution to investors is still a problem that is often debated and prominent in the company [3]. In this regard, the dividend payment policy is of particular concern, so this study seeks to optimize the dividends paid by the company/investors, thereby stimulating external sources of company funding [4].

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The company is a conflict of interest (agency conflict) and if left unchecked there will be a crisis of confidence in the company [5]. Conflicts of intesrest can occur in all companies, including sharia companies. Agency conflict between managers and investors is undeniable in companies that have excess funds [6]. Specifically, this difference in interest is caused because managers are more aware of internal information within the company than investors, this imbalance of information between managers and investors allows managers to optimize their satisfaction by giving up investor satisfaction [7].

To control dividends and be more consistent, several studies have looked for several factors that influence it and which are very dominant, namely corporate governance which is closely related to the company's dividend payment policy [8][9][10][7]. Companies with low corporate governance and complex agency problems are unable to protect minority shareholders so that they distribute minimal dividends [11][12][13].

Governance mechanisms in increasing dividend payments can be measured by institutional ownership, board of directors, and independent commissioners [14][15][16]. Institutional investors have stronger monitoring incentives to reduce agency problems because they get greater benefits from supervision to reduce the risk of information being less open by managers to investors [6][17]. The experience, insight, and more knowledge possessed by the board of directors will have an impact on a good performance. This of course gives a positive signal to the profitability of companies with high profits, the company will likely distribute dividends [18]. The experience, insight, and more knowledge possessed by the board of directors will have an impact on a good performance. This of course gives a positive signal to the profitability of companies with high profits, the company will likely distribute dividends [19][20][21] conducting studies related to the size of the company able to have a strong influence on dividend payment policies. However, there are still contradictory findings on the influence of these four factors on dividend payment policy [22][23][24][25].

2 Hypothesis Development

2.1 Agency theory

In general, agency theory can be said as a theory that describes an explanation of the relationship between principals and agents. Jensen and Meckling [26] stated that this theory explains the agency relationship and the problems it causes. the relationship between the agent and the principal can be intended as an agreement between one or many parties (principal) to another party (agent) which is intended to carry out services that will be of interest to the principal and to be involved in making decisions on the delegation of part of the authority to the agent.

2.1.1 Institutional Ownership and Dividend Policy

Institutional Ownership has a strong relationship to corporate governance and in particular, influence reducing agency costs [2], Cheng et al. [6] revealed that the greater the share ownership they have, the greater the role and discretion they have, especially regarding monitoring of corporate governance. this is done with the aim of maximizing dividend payments to investors. The results of the study [22] found no evidence that institutional ownership causes US companies to increase dividends.

H1: Institutional Ownership has positive effect Dividend Policy.

2.1.2 Board of Directors and Dividend Payment Policy

The board of directors has a role as a shareholder and is considered the main decision-making group, the complexity of decision-making and most of its effectiveness is influenced by the size of the board [27]. Board size is an important factor affecting company performance. However, theoretical explanations disagree in supporting the effectiveness of large and small board sizes on firm performance. The resulting hypothesis explains that a larger board has a more effective ability to control and monitor opportunistic behavior carried out by management. This is associated with more capabilities and experience that can anticipate agency problems and optimize company performance, one of which is dividend payments [28].

H2: The Board of Directors has a Positive effect on the Dividend Policy.

2.1.3 Independent Commissioner and Dividend Payment Policy

Rajput and Jhunjhunwala [29] explains that in terms of securing and protecting all interest activities carried out by shareholders and legislature considers giving dividends an alternative to increase the independence of the board to achieve good governance within the company the good one. According to regulations issued by the regulator namely the Financial Services Authority (OJK) Number 33/POJK.04/2014, explain that the number of independent commisioners is at least 30 percent of the total number of commissioners. Several previous studies have examined the impact of board independence on agency problems [30][31][32] and they found that the appearance of independent members on the board reduces agency problems by influencing dividend payments.

H3: Independent board has a positive effect on the Dividend Policy.

2.1.4 Company size, corporate governance and dividend policy

One of the most important indicators that can influence a company's dividend payment policy, apart from the mixed results regarding the nature of the effect, is the Size Life cycle theory of dividends predicts that the relationship between size and dividend payout is positive and significant [33]. Consistent with the predictions of life cycle theory, several previous studies have proven a positive relationship between cash dividends and size [34][35][36][37]. This is also in line with Baker and Kilincarslan [38] which proves that large company sizes tend to pay cash dividends.

H4: Firm Size Mediates the Relationship of Corporate Governance to Dividend Policy.

3 Method

This study uses descriptive and quantitative methods. The research population is all companies listed on the Jakarta Islamic Index and published an annual report for the period 2010-2019 (10 years) totaling 300 observations. Samples were taken using the purposive sampling technique and calculated based on dividend payments made so that a total sample of 217 observations was obtained. The research data is secondary data in the form of annual reports collected by electronic documentation method from the Indonesia Stock Exchange (IDX) and the company's website. Measurement of the variable dividend payout policy is proxied by Dividend Payout Ratio (DPR), Institutional Ownership is proxied by total institutional share ownership, the board of directors is proxied by total directors, independent commissioners are proxied by total independent commissioners, and company size is proxied by Ln Total Assets. The data analysis technique is descriptive analysis to determine the average level of all variables and path analysis using the PLS-SEM (Partial Least Square Structural Equation Modeling) method with WarpPLS 7.0 software to determine the influence of independent factors or variables.

4 Result and Discussion

4.1 Result

Testing the model with WarpPLS 7.0 shows an, the Goodness of fit (GoF) value of 0.332 (medium), it means that the model used in this research was relatively adequate and ideal. In addition, the Average VIF (AVIF) and Average Full Collinearity VIF (AFVIF) values were obtained, which were 1.609 and 1.751, respectively, indicating a fit result because it was under the specified conditions 5. Then the SPR value of 0.100 is acceptable because 0.7, From this value, it is understood that there are 100% paths in the model that is free from the Simpson paradox. The RSCR value of 1,000 means that it is ideally declared fit because 0.9. From the RSCR value, it was found that the participation of the R-squared was positive for 100% of the total participation of the absolute R-squared in the model. Then the SSR value of 1,000 is declared fit because 0.7. This indicates that 100% of the paths in the model are free from statistical emphasis. The NLBCDR value of 0.9 means that it is fit because the conditions for acceptance are ≥0.7. Based on the results of testing the model, this research model can be accepted. Furthermore, the results of hypothesis testing are shown in Table 1 and Fig. 1.

Table 1. Hypothesis Test Result

Independent and Moderating Variable	Dependent variable: DPR			Result
	Coeff.	Std. Error	P Value	
Independent variables				
INOW	0.112	0.067	0.048**	Significant
BDSZ	0.060	0.068	0.187	Insignificant
BIND	-0.224	0.066	<0.001***	Significant
Moderating Variable				
SIZE*INOW	0.105	0.067	0.060*	Moderating
SIZE*BIND	0.062	0.068	0.182	Inmoderating

Note: *statistically significant at 10%;**significant at 5%; *** significant at 1%.

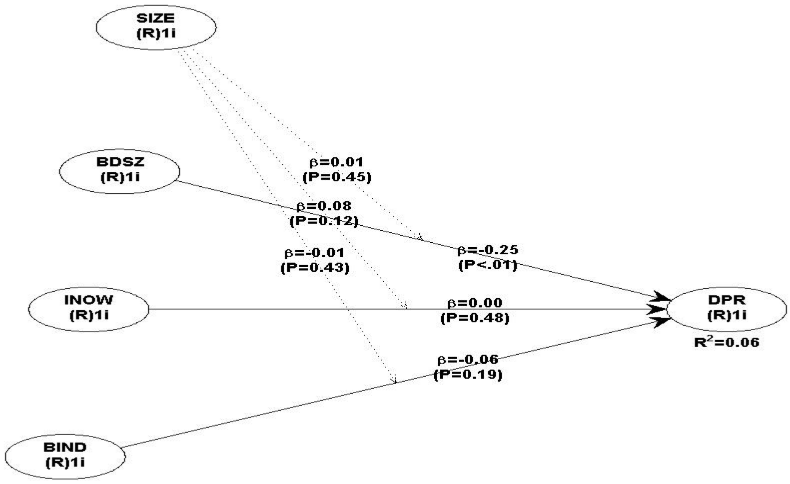

Fig. 1. Path Test Result

The results of the hypothesis testing above can describe the path coefficient values of each variable and the decision to accept or reject the hypothesis as follows:

1. The path coefficient value of Institutional Ownership (INOW) on Dividend Policy (DPR) is 0.112 with a p-value <0.048. This means that INOW has a positive and significant effect on the DPR. Then the first hypothesis (H1) is accepted.
2. The path coefficient value of the Board of Directors (BDSZ) to Dividend Policy (DPR) (DPR) is 0.060 with a p-value = 0.187 which is >0.005. This means that BDSZ does not affect the DPR. Then the second hypothesis (H2) is rejected.
3. The path coefficient value of the Independent Commissioner (BIND) on the Dividend Policy (DPR) is -0.224 with a p-value <0.001 which is <0.005. This means that BIND has a negative and significant effect on ISR. Then the third hypothesis (H3) is rejected.
4. Path coefficient value. Firm size moderates corporate governance as proxied by Institutional Ownership of Dividend Policy (DPR) which is 0.105 and p-value = 0.060 < 0.100. This means that H4 is accepted (Moderating). Meanwhile, the size of the company moderates corporate governance which is proxied by independent commissioners on the dividend payment policy (DPR) which is 0.062 and p-value = 0.060 < 0.182. This means H4 is rejected (not Moderating).

4.2 Discussion

The results of the study show that institutional ownership (INOW) has a significant positive effect on the Dividend Policy which is proxied by the Dividend Pay-out Ratio (DPR). This means that the greater the percentage of share ownership by institutions in a company, the greater the influence in increasing dividend payment decisions. Broad institutional ownership will further enhance supervision and monitoring of the performance of the company management because it is considered to have broad rights in limiting management behavior which is likely to be more selfish (opportunistic) so that it will encourage more open financial reporting on its achievements and of course this will maximize dividend distribution.

The results of the study indicate that the Board of Directors (BDSZ) does not affect the Dividend Policy which is proxied by the Dividend Pay-out Ratio (DPR). The large or small number of the board of directors in a company is not able to increase dividend payments because there is no full capacity/right for the directors to make policies, one of which is the decision to pay dividends. A larger board is considered ineffective in monitoring managerial opportunism because it is often associated with more there are many problems in communication and coordination, and thus the governance structure will be poor [39][40]. This is reinforced by the findings shown by Setia-Atmaja et al. [16] who obtained the result that board size does not have a strong impact on dividend payments in Australian companies in the period 2000-2005.

The results of the study show that institutional ownership (INOW) harms the Dividend Policy which is proxied by the Dividend Pay-out Ratio (DPR). The presence of an independent commissioner in a company acts as a party that oversees the performance of company management, protects the interests of small (minority) investors, and has a responsibility to maintain the continuity of the company's business activities. Based on that, of course, the independent commissioner considers the risks of every decision he makes. So that the decision he made not only protects investors, especially the minority, but more than that, what is very crucial is the survival of the company. This result is in line with the results of research conducted by Abdelsalam et al. [41] which found negative results for the DPR. The presence of independent commissioners can weaken the level of dividend payouts because independent commissioners are considered to be very careful in carrying out dividend payment policies and they will prioritize the company's condition to remain stable first. In addition, research Elmagrhi et al. [42] stated negative results related to the relationship of the Independent Board of Commissioners to the dividend payment policy.

Based on the results, it shows that SIZE can only mediate the relationship between INOW and DPR, this is based on the acquisition value of = 0.105 and p (0.060). meaning that if BDSZ increases by 1%, then the DPR will increase by 10.5% mediated by SIZE with the assumption that other variables outside the study are constant. the p-value is $0.060 < 0.100$ which means that SIZE mediates the relationship between INOW and DPR. As for the BIND variable, the p-value is $0.182 > 0.100$, meaning SIZE does not mediate the relationship between BIND and DPR. Institutional Ownership as a party that oversees and also contributes to decision-making, one of which is the decision to increase dividend payments if the company has a large company size which is reflected in large asset ownership. This is in line with Baker and Kilincarslan [37] which proves that large company sizes tend to pay cash dividends. Companies with large assets, of course, have maximum growth and can be said to have reached the maturity stage and have been able to generate more sources of funding internally so that they are likely to distribute the excess funds to investors

5 Conclusion and Implication

From the results of the research, the factors that affect it are found, namely corporate governance, namely institutional ownership (INOW) which shows a positive effect, and Independent Commissioner (BIND) harms dividend payment policy (DPR). The board of directors (BDSZ) does not affect. The moderating relationship shows that company size can moderate the relationship between institutional ownership (INOW) and dividend payment policy (DPR) and does not moderate the relationship between Independent Commissioners (BIND) and dividend payment policy (DPR).

This result has implications for the dividend payment policy for Sharia companies that the company's management must evaluate the obstacles that cause the inconsistency. Based on the results, it is known that institutional share ownership and independent commissioners are declared influential. So companies need to improve both of these factors by increasing the number of independent commissioners to oversee management performance to create optimal profits by attracting institutional investors to invest.

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