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Antecedent Variables of Dividend Policy in Public Manufacturing Companies:Case in Indonesia

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Abstract

The purpose of this study was to determine the antecedent variables of dividend policy. The independent variables are earnings management, managerial ownership, and free cash flow. The sample was taken by using a purposive sampling technique consisted of 302 firm years. Data collected from the Indonesia Stock Exchange with the research period from 2015 - 2018. The results of this study showed that earnings management and managerial ownership do not influence the dividend payout ratio. Free cash flow has a significant influence on the dividend payout ratio. Managers do not use free cash flow as a policy that tends to decrease shareholders' wealth. Management uses free cash flow as a policy to minimize agency costs.

Keywords: earnings management, managerial ownership, free cash flow, dividend payout ratio

1. Introduction

Dividends are the distribution of profits on investment in the form of shares in the company, the number of dividends to be distributed depends on the size of the company's profits and the dividend distribution policy that has been set by the company. Dividend politics is concerned with determining the distribution of earnings between the use of income for dividend payments to shareholders or use within the company or income that must be retained in the company (Riyanto, 2011).

An agency relationship is a contract in which principals involve agents to perform certain services on behalf of the principal who gives the agent authority to make the best decisions for the principal (Jensen & Meckling, 1976). Conditions that occur between management as an agent and shareholders or stockholders because the separation of ownership and management functions causes differences in interests. The management wants the profit earned by the company to be used for company expansion, while the shareholders want a return on the investment made in the form of dividends. This difference in interests results in conflict, in financial theory conflict caused by an agency relationship is also called agency conflict. A company that separates the management function from the ownership function will be vulnerable to agency conflicts.

Earnings management is the selection of accounting policies or certain activities by management that can affect earnings so that the reported earnings are following the wishes of the management (Scott, 2015). With such a great deal of attention to earnings, it is not surprising that corporate management takes a vital interest in how earnings are reported. In general, profit is often used as a measure in assessing the business performance of a department or its managers to the company as a whole (Gumanti, 2000). It presents the idea of earnings management which uses accounting choices to improve earnings reports for the benefit of managers. By carrying out earnings management, managers can influence the informative level of earnings which in this case can be the basis for dividend payment decisions to shareholders. Earnings management is carried out by managers, one of which is to achieve the profit expected by investors.

Managerial ownership is also the shareholder of the company. They have many company stocks. Managers will align their interests as managers and shareholders also. If without managerial ownership, managers are likely to make decisions that will tend to benefit themselves.

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Free cash flow can describe the financial condition of a company. Free cash flow is the cash left over after carrying out all projects that resulted in a positive net present value when discounted at the relevant cost of capital. The conflict of interest between shareholders and managers on payment policies becomes severe, especially when the organization generates sizeable free cash flow (Jensen & Meckling, 1976).

In previous research on the influence of earnings management on dividend policy, Srikanth (2015) proved that earnings management has a significant influence on dividend policy. Another research on dividend policy is that dividend policy is influenced by managerial ownership. However, this result is different from Haryadi's (2014) research which concluded that agency cost, which is proxied by using managerial ownership ratio, does not have a significant influence on dividend policy. Another variable that influences dividend policy is free cash flow which as in Issa's research (2015) and Aristantia's (2015) research that free cash flow has a positive and significant influence on dividend policy.

The selection of manufacturing companies listed on the Indonesia Stock Exchange (IDX) as a research sample is based on the consideration that manufacturing companies with basic and chemical industry sectors, various industries, and the consumer goods industry are companies that have the highest dividend payout ratio in 2015. In 2015, the average dividend payout ratio to shareholders by 3 sectors of manufacturing companies was 36%. The sample of financial statements was selected during the 2015-2018 financial reporting period to obtain the most recent information. The purpose of this study was to determine the influence of earnings management, managerial ownership, and free cash flow on dividend policy.

2. Theoretical Review

The dividend payout ratio is a decision to determine how many parts of the company's revenue will be distributed to shareholders and which will be reinvested or retained in the company. From this definition, the dividend payout ratio is based on a range of considerations between the interests of shareholders on the one hand, and the interests of the company on the other (Mulyono, 2009).

Earnings management is the selection of accounting policies or certain activities by management that can affect earnings so that the reported earnings are following the wishes of the management (Scott, 2015). There are two types of earnings management, namely efficient earnings management and opportunistic earnings management.Efficient earnings management is earnings management that aims to increase the informative level of earnings in communicating information originating from within the company. Opportunistic earnings management is earnings management that aims to maximize management utility, such as bonuses received by managers.

This study uses the revenue discretionary model in measuring earnings management introduced by Stubben (2010). Stubben developed a model that uses the main component of revenue, namely accounts receivable, to predict earnings management. In this study, Stubben proved that the revenue model has a lower bias, is more specific and stronger than the accrual model.

There are two formulas in the revenue discretionary model that are used to measure earnings management. First, is the revenue model, which focuses on income that has a direct relationship with accounts receivable. Second, namely the conditional revenue model, this model is being redeveloped with the addition of company size (size), company age (age), and gross margin (GRM), which are thought to be used in detecting accrual earnings management regarding credit disbursement related to accounts receivable. Firm size is a proxy for financial strength, company age is a proxy for the company's stage in the business cycle. And gross margin as a proxy of the company's operational performance with competing companies.

Influence of Earnings Management on Dividend Policy

Earnings management is the selection of accounting policies or certain activities by management that can affect earnings so that the reported earnings are following the wishes of the management. Earnings management is carried out by managers, one of which is to achieve the profit expected by

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shareholders. By carrying out earnings management, managers can influence the informative level of earnings, which in this case can be the basis for decisions on dividend payments to shareholders.

According to Kasanen et. al. (1996) dividends are influenced by earnings management. Major institutional shareholders demand high returns on their shareholdings and thus expect smooth dividend flows. This motivates the company for earnings management to show a sufficiently high income for dividend payments. To that end, reported income is dependent on dividend-based income targets.

The level of earnings management has a negative influence on dividend payments, this is following the research of Srikanth (2015). The dividend payment will discourage companies from reporting artificial profits that do not result in actual cash flow realization to support cash dividends. This means that if the company does too much earnings management, the company will pay low dividends.
H1 predicts earnings management influences dividend policy.

Influence of Managerial Ownership on Dividend Policy

In the agency cost hypothesis, dividend payments to shareholders can serve to align interests and reduce agency problems between managers and shareholders. Rozeff (1982) argues that high managerial ownership causes a low dividend payout ratio. The determination of the low dividend is due to the manager's expectation of future investments that are funded internally. If some shareholders like high dividends, this will create differences in interests so that an increase in dividends is needed. Conversely, if there is a common preference between shareholders and managers, there is no need to increase dividends.

The results of the study of Mangantar and Sumanti (2015) show that managerial ownership has a significant influence on dividend policy. This occurs due to companies that have managerial ownership values or companies in which some commissioners and directors play an active role in decision making to get equal with other shareholders who tend to pay high dividends for the welfare of shareholders under the main objective of a company is doing business.
H2 predicts managerial ownership influences dividend policy.

Influence of Free Cash Flow on Dividend Policy

Free cash flow can describe the financial condition of a company because companies with high free cash flow are considered capable of facing bad conditions. Free cash flow is the residual cash flow from financing all projects that produce a positive net present value (NPV) and are discounted at the relevant cost of capital. Agency problems will get worse when the company generates large amounts of free cash flow. According to the agency cost hypothesis, the available free cash flow in large enough quantities in a company usually creates conflicts due to differences in interests between managers and shareholders. According to Posner (2009), the influence of free cash flow on the dividend payout ratio is positive, which means that the higher the free cash flow, the higher the dividend payout ratio or the lower the free cash flow, the lower the dividend payout ratio.

Aristantin and Putra's (2015) research results show that free cash flow has a positive influence on the level of dividend payment. Companies with large free cash flow will get pressure from shareholders on managers to pay dividends. This is done so that managers do not use free cash flow as a policy that tends to harm shareholders. So that management uses free cash flow as a policy to minimize agency costs.
H3 predicts free cash flow influences dividend policy

3. Research Methods

This research is empirical study research on manufacturing companies listed on the Indonesia Stock Exchange in 2015-2018. This research uses quantitative data types and uses secondary data sources. Secondary data used are the 302 company's financial statements published on the IDX website.

Population and Sample

The population of this research is all manufacturing companies listed on the Indonesia Stock Exchange (IDX). Sampling was done by using a purposive sampling method, which is a sampling method based on certain criteria. The criteria for taking the research sample were determined as follows: manufacturing

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companies listed on the IDX that published their financial reports in succession from 2015-2018, distributed dividends in succession from 2015-2018, provided financial reports presented in complete rupiah currency from 2015-2018, has complete financial data needed in this study.

4. Results and Discussion

Multiple Linear Regression Analysis

Multiple regression analysis in this study aims to estimate or predict the influence of discretionary accrual, managerial ownership, and free cash flow on the dividend payout ratio.

Table 1. Hypotheses Test Result

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.467	0.031		14.082	0 000
DR	- 0.016	0.030	- 0.046	- 0 527	0.599
OWN	0.350	0.211	0.145	1.066	0.100
FCF	0.307	0.113	0.236	2.071	0.008

Source: processed data, 2020

Hypothesis Testing

Hypothesis testing in this study is used to test the previously formulated hypotheses and to determine the influence of the independent variable on the dependent variable with t-test an analysis of variances (F-test).

The t-test is a statistical test to determine whether the independent variable individually influences the dependent variable. If the probability level is less than 0. 05, it can be said independent variables affect the dependent variable.

Based on the results table 1 above t statistical test, discretionary accrualhas a p-value = 0.599> 0.05, which means that discretionary accrualdoes not affect the dividend payout ratio. Managerial ownership has a p-value = 0.100> 0.05, which means that the partial managerial ownership does not affect the dividend payout ratio.Free cash flow has a significance value of 0.008 < 0.05, which meant that free cash flow is a positive and significant influence on dividend payout ratio.

Table 2. Analysis of Variance

Model	Sum of Squares	Mean Square	F	Sig.
Regression	1.123	0.374	3.465	0.018 [b]
Residual	13.069	0.108		
Total	14.192			

Source: processed data, 2020

F test is to determine whether the independent variables affect the dependent variable. If the probability level is less than 0.05, it can be said that all independent variables together influence the dependent variable. The level of significance of F = 0.018 < 0.05, so that it can be interpreted that all independent variables (discretionary accrual, managerial ownership, and free cash flow) simultaneously influence the dependent variable (dividend payout ratio).

The coefficient of determination (Adjusted R2) is used to determine how far the model can explain the variation in the dependent variable.Based on the results testing, the Adjusted R-value is 0.057. These results indicate that only the independent variables can explain the dependent variable variation is 5.6%.

4.1 Discussion

The Influence of Earnings Management on Dividend Policy

The results of multiple linear regression analysis of earnings management do not influence dividend policy because it has a p-value = 0.599 with a regression coefficient of -0.018. These results

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indicate that the company does earnings management, not to influence dividend policy decisions by shareholders. Several reasons motivate managers to carry out earnings management and in this case, managers are influenced by the interests of managers to maximize management utility, such as opportunistic earnings management.

The results of data analysis in this study showed that managerial ownership has no significant influence on dividend policy dividend because it has a p-value = 0.100 with a regression coefficient of 0.350. This can be caused by managers acting according to shareholder preferences (convergence of interest hypothesis). With this common preference, shareholders do not need to increase dividend payments even though the percentage of ownership by managerial is low.

The results in this study indicate that free cash flow has a significant and positive influence on dividend policy because it has a p-value = 0.008 with a regression coefficient of 0.307. Companies with large free cash flow pay bigger dividends. This is done so that managers do not use free cash flow as a policy that tends to decrease shareholders' wealth. Management uses free cash flow as a policy to minimize agency costs.

5. Conclusion

Based on the results of the analysis in this study, it can be concluded that discretionary accrual, managerial ownership, do not influence the dividend payout ratio, while free cash flow has a significant influence on the dividend payout ratio. The suggestions that researchers can give in this study are for future researchers to add other factors that affect dividend policy in the model used in the study because the coefficient of determination in this study is quite low. Further researchers are also expected to expand the scope of sample selection by including companies that have paid dividends during the study period.

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