

# Institutional Investors and Firms' Cash Dividend Payments: Evidence from Non-Financial Firms in Indonesia

*(Pelabur Institusi dan Pembayaran Dividen Tunai Firma: Bukti dari Firma Bukan Kewangan di Indonesia)*

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## ABSTRACT

*This paper investigates whether an institutional presence influences the level of a firm's cash dividend payments. Using data from all non-financial firms listed on the Indonesian Stock Exchange (IDX) during the research period of 2010 to 2015, this research performs regression analysis. The results show that institutional investors can influence cash dividend payments. However, different types of institutional investors have different impacts on dividends. While foreign investors have a significant impact on the level of dividends, local institutional investors do not have a significant effect. Also, this research reveals that free cash flow and leverage have a negative influence on cash dividend policies, while firm size, market-to-book value of equity, and return on assets have a positive influence on cash dividend policies.*

*Keywords: Institutional investor; dividends; Indonesian Stock Exchange (IDX)*

## ABSTRAK

*Kajian ini menyoal sama ada kehadiran institusi bebas mempengaruhi tahap pembayaran dividen tunai firma. Menggunakan data semua syarikat bukan kewangan yang tersenarai di Bursa Saham Indonesia (IDX) bagi tempoh penyelidikan 2010 hingga 2015, kajian ini melakukan analisis regresi. Hasilnya menunjukkan bahawa pelabur institusi bebas boleh mempengaruhi pembayaran dividen tunai. Walaubagaimanapun, perbezaan jenis pelabur institusi mempunyai kesan yang berbeza ke atas dividen. Selain itu, pelabur institusi bebas asing mempunyai keupayaan yang lebih besar dan lebih banyak insentif untuk mempengaruhi pembayaran dividen tunai berbanding pelabur institusi bebas tempatan. Kajian ini juga menunjukkan bahawa aliran tunai bebas dan leveraj mempunyai pengaruh negatif ke atas dasar dividen tunai, manakala saiz firma, nilai pasaran-kepada-nilai buku bagi ekuiti dan pulangan ke atas aset mempunyai pengaruh positif terhadap dasar dividen tunai.*

*Kata kunci: Pelabur bebas; dividen; Bursa Saham Indonesia (IDX)*

## INTRODUCTION

Institutional investors have become the leading players of corporate governance reform across the globe (International Monetary Fund 2016). Previous researchers found that institutional investors can influence the firm level of governance (Aggarwal et al. 2011) and have a significant impact on firm values in several countries (Ferreira & Matos 2008). This includes emerging countries, i.e. Latin America countries (De-la-Hoz & Pombo 2016). These results indicate that the monitoring performed by institutional investors optimizes administrative performance.

Previous studies have highlighted the role of institutional investors on promoting corporate governance reform in emerging countries (e.g. Ward, Yin & Zeng 2018). Institutional investors are recognized for balancing the power of majority shareholders in their effort to maximize the shareholder value they represent by reducing agency problems (Gillan & Starks 2003). One of the corporate governance tools to deal with agency problem is paying out a cash dividend to minimize the free cash flow under management's discretion (Jensen 1986). Research by Short, Zhang and Keasey (2002) and Firth et al. (2016) confirmed this theory. Those researchers concluded that there is a positive relationship between institutional ownership and dividend payout policies as a tool to reduce agency problems. The presence of institutional ownership encourages higher dividend payouts to minimize the excess free cash flow at the discretion of management that might otherwise be invested in a negative net present value project.

TABLE 1. Development of mutual fund products in Indonesia

Period	Number of Mutual Fund Products
December 2016	1,425
December 2015	1,091
December 2014	894

Today, Indonesia faces an increase in the role of the institutional investors, and the Indonesian capital market is dominated by foreign entities (see Table 2). These two elements are in line with global events; in fact, the role of institutional investors (especially mutual funds and pension funds) in the Indonesian equity market has increased in the last five years. From Table 1, we can see that the number of mutual fund products in Indonesia has grown rapidly in the last three years and that the total value of institutional ownership has increased from 17.73% in 2012 to 22.33% in 2016 (Financial Services Authority (OJK) 2016).

TABLE 2. Institutional investor development (2012 vs. 2015)

Ownership By	2015		2012	
	Value of Equity Securities (trillion Rupiah)	%	Value of Equity Securities (trillion Rupiah)	%
Foreign Mutual Fund	356.86	11.50%	261.07	10.34%
Local Mutual Fund	129.04	4.16%	89.88	3.56%
Foreign Pension Fund	137.76	4.44%	71.54	2.83%
Local Pension Fund	69.57	2.24%	25.23	1.00%
<b>Total Institution Ownership</b>		<b>22.34%</b>		<b>17.73%</b>
Total Equity Owned by Foreign Entities	1,691.35	54.49%	1,484.39	58.79%
Total Equity Owned by Local Entities	1,412.53	45.51%	1,040.62	41.21%
<b>Total Equity Securities</b>	<b>3,103.88</b>	<b>100.00%</b>	<b>2,525.01</b>	<b>100.00%</b>

This research aims to analyze whether institutional investors can influence the dividend payout policy. The research aims to contribute to the discussion on the agency problem perspective that highlights the potential of conflict of interest arising from excess free cash flow. According to Claessens and Yurtoglu (2013), studies on the role of institutional investors in discipline management in emerging markets are scarce, and no solid evidence of their behavior is available. Moreover, the results are still inconclusive. Some researchers found that foreign investors positively influence dividend payment (e.g. Kim & Sul 2010; Cao, Du & Hansen 2017). Meanwhile, Jacob and Jijo Lukose (2018) showed a different result, that there is no evidence to support a positive relationship between institutional investor ownership and dividend payment payout level.

The previous research in Indonesia has revealed a positive significant relationship between institutional ownership and dividend payout policies in manufacturing industries in (Embara, Wiagustini & Bagus 2012) Indonesia. A more recent study in Indonesia by Kurniawati, Manalu, and Octavianus (2015) concluded also that there is a positive significant relationship between institutional ownership and the dividend payout policies in the real estate industry in Indonesia. However, those studies were limited to specific industries. Thus, further research that applies data from all industries is needed.

Moreover, this research focuses also on the difference between local and foreign institutional investors in influencing dividend payments. Investigating the difference between local and foreign independent ownership is interesting, because previous studies have shown that foreign and institutional investors are better at monitoring companies. In fact, foreign and institutional investors have been proven to export good corporate governance around the world, especially foreign institutional investors from countries with strong shareholder protection (Ferreira & Matos 2008; Aggarwal et al. 2011). Research uncovered evidence also that foreign investors positively influence dividend payout policies in China (Cao et al. 2017) and Korea (Kim & Sul 2010). Since dividends can be used as a tool to reduce agency problems, it is interesting to investigate whether foreign investors (especially foreign institutional investors) can positively influence dividend payout policies as a means to reduce agency problems. Indonesia provides a suitable context in which to test the different roles of domestic and foreign institutional investors. There is a high concentration of ownership in Indonesian companies associated with a group of family companies. The founders of Indonesian companies tend to retain their majority shares so that they can retain control over the management, either directly or through holding companies as mentioned above (Mouna Wasef & Retno 2010). Some researchers surmise that institutional investors represent family holding companies that have a strong affiliation with a firm's management. Although domestic institutional investors pose significant influence in Indonesia, they have failed to promote corporate governance reform because they have strong affiliations with management (Sugeng 2009). This research will provide new information regarding the weakness

of domestic institutional investors in affecting managerial decisions since they could have strong affiliations with major shareholders.

This research focuses on the difference between local and foreign institutional investors in influencing dividend payments. Investigating the difference between local and foreign independent ownership is interesting because the previous studies have shown that foreign and institutional investors are better at monitoring companies. In fact, foreign and institutional investors have been proven to export good corporate governance around the world, especially foreign institutional investors from countries with strong shareholder protection (Ferreira & Matos 2008; Aggarwal et al. 2011). Research by Cao et al. (2017) and Kim and Sul (2010) found evidence also that foreign investors positively influence dividend payout policies in China and Korea, respectively. Since dividends can be used as a tool to reduce agency problems, it is interesting to investigate whether foreign investors (especially foreign institutional investors) can influence dividend pay-out policies as a means to reduce agency problems.

## LITERATURE REVIEW

The existence of agency problems is inevitable in modern companies due to the development of global capital markets. The number of individuals and corporations who invest their money in a company's stock through capital markets has increased rapidly. These investors expect their wealth to increase as the company grows over time. However, not every investment produces favorable results. Several large cases like that of Enron, Goldman Sachs, and Bernie Madoff have revealed the very high cost of agency problems. These cases illustrate the importance of corporate governance to prevent such occurrences in the future. Gillan and Starks (1998) define corporate governance as the systems of law, rules, and factors that control the operations of a company. A firm's governance consists of the set of structures that provide boundaries to every party involved in the firm's operations and to the benefits or returns they receive. In another paper, Shleifer and Vishny (1997) emphasized the economic interests of every party by defining corporate governance as the ways in which those who supply financing to companies ensure that they receive a return on their investment.

Around the world, both international and domestic institutional investors are the top suppliers of external funding. As suppliers of external funding, institutional investors have played an important role in reforming corporate governance (International Monetary Fund 2016). A study by Gillan and Starks (2003) concluded that institutional investors, including professional money managers, offer better company monitoring than individual shareholders, because they possess significant ownership of a company and have the incentive and the financial means to rigorously monitor the company.

Beyond monitoring, institutional investors also have the potential to exercise control over a company's management, either directly through the board of directors or indirectly by refusing to invest in a company, thus increasing a company's cost of capital (Gillan & Starks 2003). This finding is confirmed by the study by Ferreira and Matos (2008), which concluded that institutional shareholders could push a company's management to fulfill their desires for better financial outcomes by directly voicing their interest during shareholders' meetings or voicing their discontent by selling their shares (known as the "Wall Street Walk").

However, the impact of institutional investors differs according to their type. A study conducted by Brickley, Lease and Smith (1988) suggested two major groups of institutional investors: the pressure-sensitive group, whose members have current or potential business with the company (banks, insurance companies, and trusts), and the pressure-resistant group, whose members have no current or potential business with the company (mutual funds, endowments, foundations, and public pension funds). That research concluded also that the pressure-resistant group (institutional investors) is more likely to oppose management than the pressure-sensitive group. Their findings indicated that the pressure-resistant group is more likely to set as its goal the overall shareholders' value maximization, since this group has fewer business relations with the company. More recent study by Borochin and Yang (2017) found that dedicated investors are associated with better governance system, while transient investors are not.

Agency theory suggests that company managers prefer to spend the company's resources on activities that benefit themselves instead of shareholders (Jensen 1986). One powerful tool to mitigate this risk is the payment of cash dividends to minimize free cash flow that would be invested in low-return projects or would be misappropriated by management. Moreover, by paying dividends, the management is also forced to seek external financing (especially debt), a method that has been proven to offer better monitoring and pressure over management (Jensen 1986). In their research, Short et al. (2002) found a positive relationship between dividend payout policy and institutional ownership. A more recent study by Firth et al. (2016) in China implied that institutional investors have the ability to exert influence on firms to pay cash dividends and to increase cash dividends as a means to reduce the agency problem that might arise due to excessive free cash flow at the management's discretion. However, study by Jacob and Jijo Lukose (2018) showed a different result. Using data of NSE-listed non-financial firms in India during the period 2001 to 2016, the research has no evidence to support a positive relationship between institutional investor ownership and dividend payment payout level.

Normally, institutional investors do not have direct input into a firm's management decisions (e.g., dividends, capital investment), as they are not represented on the board of directors. However, institutional investors have several ways to exert influence through both direct and subtle means (Firth et al. 2016). Institutional investors can challenge top executives on corporate strategies and operations and can express their views regarding the firms through attendance and voting at the annual general shareholders' meeting. Subtler means of influence include the threat of exit. According to the clientele theory, an investor chooses to invest in a company due to specific company policies that satisfy its preferences, and if a company changes its policies (in this case, dividend payment level), investors can adjust their stock holdings. Therefore, if an institutional investor feels that the company is no longer satisfying its preferences of high dividend payment, it might sell its stock holdings. Moreover, if an institutional investor sells its shares, it creates negative connotations for the firm's stock price, since the institutional investor is perceived by the capital market as being an expert investor who will only sell shares if he or she believes a firm is overvalued and has poor long-term prospects. To avoid this occurrence, the firm will try to appease the institutional investor by listening to its advice during the annual general shareholders' meeting and by increasing dividend payouts.

Due to globalization, foreign investors have a large influence on equity markets in emerging countries. Thus, for emerging countries like Indonesia, the group is divided further into local and foreign pressure-sensitive groups and local and foreign pressure-resistant groups. Due to the varying backgrounds and affiliations with the countries in which they invest, foreign and local institutional investors have different perceptions of corporate governance. Since investors prefer to invest in firms with good corporate governance, many firms are motivated to improve their corporate governance practices to attract foreign investors. Subsequently, increased foreign investor ownership enforces further governance reform (Gillan & Starks 2003). Another study conducted by Ferreira and Matos (2008) implied that foreign and pressure-resistant institutional investors can better monitor companies. Aggarwal et al. (2011) concluded that international investors export good corporate governance around the world, especially foreign institutional investors from countries with strong shareholder protection.

Moreover, recent research in Asia suggested that foreign institutional investments have a positive relationship with dividend policies. Research by Kim and Sul (2010) revealed that foreign institutional investors (with more than five percent ownership) have a significant positive impact on dividend payments; this implies that foreign institutional investors are determinants of corporate dividend policy as a means of monitoring. Research by Lahiri (2013) suggests that foreign institutional investors have a positive significant impact on dividend policies in India. More recent research by Cao et al. (2017) found that, in China, foreign institutional investors positively influence dividend payments, which implies that foreign institutional investors could demand higher dividend payment from firms in which they invest to minimize agency problems. Therefore, those studies concluded that foreign institutional investors have a greater positive relationship on dividend policies compared to domestic institutional investors.

## RESEARCH METHOD

### DATA

This research examines all of the companies listed on the Indonesian Stock Exchange (IDX) during the research period of 2010 to 2015, excluding companies in the financial services industries (e.g., bank, securities companies, and insurance companies). To avoid the effect of global financial crises in 2008-2009, we start the sampling period in year 2010. The sample excludes companies in financial services industries, since they are highly leveraged and have specific accounting and regulatory standards and hence are not comparable with other companies. In determining industry classifications, the researchers used Thomson Reuters Business Classification (TRBC), an industry classification system based on the market a company serves (Thomson Reuters 2016a, 2016b).

In selecting which companies to include in the sample, two criteria were applied. First, the company must have been listed before the research period to ensure that available data regarding institutional holdings can be found on the KSEI database. Second, the company must have a complete dataset for all of the variables being examined. Ultimately, 337 companies fulfilled the criteria, providing a total of 2,022 firm-year observations.

The study collected financial statements data from Thomson Reuters' Eikon terminal. This database provides access to trusted, up-to-date, and accurate financial statements data for 99% of the companies listed in the world, including Indonesia (Thomson Reuters 2016a, 2016b). For institutional holding positions for each period end, data were collected from the Indonesian Central Securities Depository (KSEI) database from its website. This database provides the holding composition position for all publicly traded shares of listed companies on the IDX for a specific date.

VARIABLE

RESULTS

Based on the sample criteria set in the previous section, there are 337 companies that fulfill the criteria, with a total of 2,022 firm-year observations. Summarized below in Table 4 are the descriptive statistics of the data used in this research. On average, the dividend payout ratio of all companies is 15.87%, which is relatively low. On average, the total institutional ownership in all companies is 3.66%. The descriptive statistics above imply that, after being winsorized at 5% of each tail to minimize the impact of outliers, all of the variables are considered normally distributed.

A series of tests were conducted to ensure the compliance of the result with classical assumptions. The first assumption to be met is that the model is free from multicollinearity problems. In testing this assumption, the study employed a VIF test. The VIF test results indicate that no multicollinearity problem exists, since the VIF test result of all independent variables is less than 10. Moreover, we also find that the correlations among independent variables are low, as we can see from the correlation matrix table (Table 5). We only find a high correlation between Variable IND and Variable FORIND or LOCIND. However, this would not be a problem since we do not use Variable IND and FORIND/LOCIND in the same model.

TABLE 4. Descriptive statistics of winsorized samples at 5% of each tail

Variable	Obs	Mean	Std. Dev	Min	Max
DIV	2022	0.1587	0.2280	0.0000	0.7693
LOCIND	2022	0.0166	0.0250	0.0000	0.0858
FORIND	2022	0.0168	0.0303	0.0000	0.1053
IND	2022	0.0366	0.0540	0.0000	0.1782
FCF	2022	-0.0039	0.0842	-0.1979	0.1429
LEV	2022	0.5369	0.2261	0.1416	0.9657
SIZE	2022	28.2057	1.5754	25.3112	30.9692
MTB	2022	1.9614	2.0916	0.0000	7.948
ROA	2022	0.0436	0.0808	-0.1185	0.2217

The second assumption to be met is that the model is free from heteroscedasticity problems. In testing this assumption, the study employed the Breusch-Pagan test. The Breusch-Pagan test result indicates that a heteroscedasticity problem does exist. The third assumption to be met is that the model is free from autocorrelation problems. In testing this assumption, the study employed the Wooldridge test, which tests the existence of autocorrelation in the panel data (Drukker 2003). The Wooldridge test result indicates that an autocorrelation problem exists.

TABLE 5. Correlation matrix

	DIV	FCF	MTB	ROA	LEV	SIZE	LOCIND	FORIND	IND
DIV	1								
FCF	-0.2011	1							
MTB	-0.0133	0.1353	1						
ROA	-0.039	0.4028	0.3951	1					
LEV	-0.0282	-0.1697	0.1295	-0.3628	1				
SIZE	-0.0206	-0.0899	0.0144	-0.0616	0.2896	1			
LOCIND	-0.0544	0.0186	-0.0094	0.0419	0.0952	0.25	1		
FORIND	-0.036	0.0505	0.2508	0.186	0.0745	0.4202	0.2313	1	
IND	-0.0548	0.0473	0.1828	0.1606	0.1045	0.4426	0.6857	0.8667	1

To determine which technique is more appropriate for data panel estimation, the researchers employ an F-restricted test, Breusch Pagan Lagrange Multiplier, and Hausman test (Suwardi 2011). The results of the test show that the more appropriate technique is the Pooled Least Square. Due to the existence of the heteroscedasticity and autocorrelation problem in the model, further treatment was required. In order to generate a value of standard error robust to heteroscedasticity and autocorrelation, (Hoechle 2007) suggests performing a Newey-West standard error estimator.

The Robust Pooled Least Squares technique employed will generate both regression results and the coefficient of multiple determinants or  $R^2$ . The result showed that, for the first model, the Adjusted  $R^2$  is 0.3121, which implies that the 31.21% of the movement of the dependent variable is explained by the movement of independent variables. For the second model, the adjusted  $R^2$  is 0.3127, which implies that 31.27% of the

movement of the dependent variable is explained by the movement of the independent variables. The low score of  $R^2$  is consistent with some previous researches (e.g. Firth et al. 2016; Cao et al. 2017). The researcher also performed a fixed-effects panel data processing technique to test the robustness of the regression result, which can be observed in Table 5.

The variable Institutional Ownership has a coefficient of -0.223 and is significant at a 95% confidence interval. The variable LOCIND (Local Institutional Ownership) has a coefficient of 0.182 and is not significant at the 95% confidence interval. The variable FORIND (Foreign Institutional Ownership) has a coefficient of 0.421 and is significant at the 95% confidence interval. The variable FCF (Free Cash Flow) has a coefficient of -0.297 and is significant at the 95% confidence interval. The variable LEV (Leverage) has a coefficient of -0.062 and is significant at the 95% confidence interval. This result implies that a decrease of one unit of FCF variable will increase the dividend payout ratio by 0.062 units. The variable SIZ (Firm Size) has a coefficient of 0.022 and is significant at the 95% confidence interval. The variable MTB (Market Value of Equity to Book) has a coefficient of 0.011 and is significant at the 95% confidence interval. Finally, the variable ROA (Return on Assets) has a coefficient of 1.373 and is significant at the 95% confidence interval.

This research reveals that institutional investors can significantly affect a firm's dividend payment decision. This finding confirms the first hypothesis predicting that institutional ownership has a positive relationship with cash dividend payment. This result is consistent with research by Short et al. (2002) that there is a positive relationship between institutional ownership and dividend payout policy. A positive relationship between institutional investor and dividend payout policy is also consistent with recent research by Firth et al. (2016), who argued that institutional investors can exert influence on firms to pay cash dividends as a means to reduce agency problems. The institutional investor's demand for higher dividend payments is given as an attempt to reduce the agency problem that might occur due to the availability of excess free cash flow at management's discretion.

TABLE 5. Newey-West regression result

	Model 1				Model 2			
	Dependent Variables				Dependent Variables			
	Newey-West Standard Error		Fixed Effect		Newey-West Standard Error		Fixed Effect	
DIV_w1	DIV_w1	DIV_w1	DIV_w1	DIV_w1	DIV_w1	DIV_w1	DIV_w1	
IND_w1	1.023*** (9.20)		0.223* (2.16)	0.240* (2.58)				
LOCIND_w1					0.521* (2.09)		0.182 (0.86)	0.190 (0.98)
FORIND_w1					1.864*** (8.50)		0.421* (2.09)	0.456* (2.57)
FCF_w1		-0.300*** (-4.00)	-0.297*** (-3.96)	-0.308*** (-4.93)		-0.300*** (-4.00)	-0.295*** (-3.93)	-0.305** (-4.90)
LEV_w1		-0.065** (-3.00)	-0.062** (-2.87)	-0.063** (-3.10)		-0.065** (-3.00)	-0.062** (-2.87)	-0.063** (-3.11)
SIZE_w1		0.026*** (8.47)	0.022** (6.57)	0.022*** (7.15)		0.026*** (8.47)	0.021*** (5.91)	0.021** (6.45)
MTB_w1		0.012*** (4.82)	0.011*** (4.24)	0.011*** (4.95)		0.012*** (4.82)	0.011*** (4.15)	0.011** (4.85)
ROA_w1		1.381*** (15.06)	1.373*** (14.78)	1.378*** (18.80)		1.381*** (15.06)	1.361*** (14.47)	1.365** (18.53)
_cons	0.121*** (17.01)	-0.619*** (-7.43)	-0.528*** (-5.75)	-0.529*** (-6.18)	0.119*** (16.42)	-0.619*** (-7.43)	-0.489*** (-5.12)	-0.488** (-5.51)
N	2022	2022	2022	2022	2022	2022	2022	2022
Adj R-sq	0.0583	0.3104	0.3121	0.3141	0.0767	0.3104	0.3127	0.3151

Notes: \* significant at 95% confidence interval, \*\* significant at 99% confidence interval, \*\*\* significant at 99,99% confidence interval, \* p<0,05, \*\* p<0,01, \*\*\* p<0,001, t statistic in parentheses

The regression results also show that the impact of foreign institutional ownership is consistent with the previous result that institutional owners have a positive relationship with cash dividend payments. We find different results for the local institutional investors. The results show that local institutional investors did not have

a significant impact on cash dividend payments. The regression results offer empirical evidence that foreign institutional investors can influence a firm's dividend distribution as a way to reduce the agency problem that might occur due with excess free cash flow at the management's discretion. The foreign institutional investor desires to protect the shareholders that it represents. This ability is proven greater compared to its local counterpart, since foreign institutional investors are more motivated to reduce agency problems, and they have better perception over governance and are actively reforming governance practice throughout the world. This result is consistent with the findings by Kim and Sul (2010) and Cao et al. (2017), which reveal a positive relationship between foreign institutional ownership and dividend payout policies.

The study predicted that local institutional investors are less motivated, since they share a common background and corporate governance perception as the companies in which they invest. Moreover, as stipulated by Capital Market and Financial Institutions Supervisory Agency (now the Financial Services Authority) Decrees No. KEP-13/PM/2002 and KEP-552/BL/2010, the maximum ownership of an Indonesian mutual fund (the largest institutional investor) in a listed Indonesian company is 5% of the paid-in capital of the company (Financial Services Authority (OJK), 2016). Due to this regulation, a local mutual fund will have lower ownership and less influence on management compared to its foreign counterpart.

The regression result implies that higher free cash flow will decrease dividend payments. This result is in contrast to the researcher's prediction and the findings of previous studies, such as Firth et al. (2016). Those researchers state there is a positive relationship between free cash flow and dividend payout policy and argue that higher free cash flow leads to higher cash dividends. This study conducted further investigation of 2,022 observations and found that 909 distribute cash dividends (have a dividend payout ratio greater than 0). Of the 909 observations that distribute cash dividends, 312 have negative free cash flow (34.32%). This occurrence confirms the stickiness of the dividend policy argument, suggesting that, once a company pays a dividend, it will maintain dividend payments, even during periods of financial stress (negative income and operating cash flow) to maintain investors' perception of a firm's prospects (Miller 2011). This researcher observes that, during this research period, due to dividend stickiness and regardless of the free cash flow condition, firms maintained their dividend levels. Therefore, there is a negative relationship between free cash flow and dividend policy, because, even when companies are facing negative free cash flow, they tend to maintain their dividend level to maintain investors' perceptions.

The regression results imply that higher leverage will decrease dividend payments. This result is consistent with the study's prediction and the findings of the previous studies. The researcher believes that this finding confirms the theory that leverage can act as a substitute for dividends in resolving agency problems. This result is consistent with findings by Kim and Sul (2010), Cao et al. (2017) and Firth et al. (2016), which observe a negative relationship between leverage and a dividend payout policy. They argue that leverage is a good substitute for cash dividends to reduce agency problems.

The regression results imply also that the larger the company size, the more dividends it will distribute. The researcher believes that larger firms are mostly mature firms that seek to maintain their reputation among investors and pay larger dividends compared to smaller firms (Dewi 2008). This result is consistent with findings by Cao et al. (2017) that there is a positive relationship between firm size and dividend payout policy. There is evidence that larger firms pay more dividends than smaller firms.

The regression results also imply that higher market-to-book value of equity (which represents investment opportunities) will increase dividend payments. This finding is inconsistent with the researcher's prediction that there is a negative relationship between the market-to-book value of equity, because companies tend to retain current earnings for investment opportunities. The researcher believes that, due to dividend stickiness, regardless of the potential investment opportunities, firms maintain their dividend levels. Therefore, there is a positive relationship between the market-to-book value of equity and the dividend policy, since even when companies have potential investment opportunities, they tend to maintain their dividend levels to maintain investors' perception of the firms' prospects. This result is consistent with findings by Firth et al. (2016), which showed a positive relationship between market to book value of equity and a firm's dividend payout policy.

The regression results imply also that the higher the ROA of the current year, the greater likelihood that a dividend will be distributed from the current year's earnings. This finding is consistent with the study's prediction. This result is consistent with the findings by Kim and Sul (2010); Cao et al. (2017); and Firth et al. (2016), which all revealed a positive relationship between ROA and dividend payout policy.

This consistency confirms that the shareholder structure of Indonesia's equity market is similar to that of other Asian countries (like Korea and China). Indonesia, like China, is dominated by controlling shareholders that are state-owned enterprises, private firms, or family firms (Firth et al. 2016). Moreover, like Korea, Indonesia has been considered an emerging market in the last decade and has a strong presence among foreign institutional investors (Kim & Sul 2010). Lastly, this finding confirms the theory that institutional investors (local and especially foreign ones) are actively reforming corporate governance practices in the Asian region (Firth et al. 2016; Kim & Sul 2010).

## MANAGERIAL IMPLICATION

The results of this research have further implications. This research reveals that institutional investors have the ability to influence cash dividend policy distribution. This implies that institutional owners have the ability to influence the decision-making process in a company. However, the consistent impact of institutional owner to dividend only apply for foreign institutional ownership. This might imply that foreign institutional investor has greater ability and incentives to influence cash dividend policy compared to local institutional investor. Moreover, foreign institutional investors might be more motivated to influence cash dividend payment as a tool to reform the governance practice of the companies they invest in. Also, this condition indicates that Indonesian institutional investors have pseudo independency due to their strong affiliation with management. This finding implies that the remaining public shareholders are minority shareholders who have weak monitoring power and cannot influence management decisions. The additional unnecessary blockholder will increase the governance in a company. This new blockholder should also be independent of the majority owner. The policy to increase the presence of foreign investors might lead to a positive impact on the governance in Indonesia.

## CONCLUSION

This study was designed to identify and test whether institutional investors influence dividend payout policies and whether there are any differences between local and foreign institutional investors' ability to influence the dividend payout policy. This research examines all firms listed on the Indonesian Stock Exchange, excluding firms operating in financial industries, from 2010 to 2015.

The study found that institutional investors have an influence on cash dividend policy distribution, either directly through annual general shareholders' meeting or by the threat to exit. Moreover, a foreign institutional investor has a greater ability and stronger incentives to influence cash dividend policies, compared to a local institutional investor. The study finds that foreign institutional investors are more motivated to influence cash dividend payments as a tool to reform the governance practice of the companies in which they invest. Influencing cash dividend policies to reduce agency problems is an example of foreign institutional activism in corporate governance reform. This study supports the belief that foreign independent investors will actively and consistently reform Indonesian corporate governance practices and that Indonesia will experience a better corporate governance climate and better minority shareholder protection in the future. This study also provides an insight that companies in country with low investor protection tend to control the companies, including using affiliated institutional investor. This situation has made the presence of institutional ownership did not always bring additional monitoring mechanisms to improve governance in the company.

This study shows also that free cash flow and leverage have a negative influence on cash dividend policies, while firm size, market-to-book value of equity- and return on assets have a positive influence on cash dividend policies. This researcher argues that the negative influence of free cash flow over dividend policy is due to dividend stickiness; this implies that, regardless of a firm's current free cash flow condition, the "implicit commitment" of its previous dividend payments can enable the company to maintain its current dividend level.

Furthermore, we suggest that future research employ the blockholder approach to explain the power of local and foreign institutional ownership in influencing cash dividend policy. Further research should also consider examination by industry and compare state-owned enterprises to non-state-owned enterprises, because different industries might have different dividend policies. By examining different groups of companies, further research can provide a better understanding of the ability of an institutional investor to influence the dividend policy.

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