

CHAPTER I INTRODUCTION

1.1 Background Research

Many researches have studied the topic on dividend and question exists on the motivation for paying dividend despite having numerous extensive research and many different models explaining the dividend behavior. In a traditional stock valuation model, dividend still plays an essential role and so we could understand it better by understanding the stock valuation model. Stocks have value as they hold future cash payouts while dividend represents the primary payments in the form of cash to the shareholders, and it normally relies on the profits earned. When we have greater expected future flow of dividends, the value of the stockholder's share will be greater too. However, some researchers argued that dividend and shareholders are directly related which means that dividend increases the shareholders wealth (Gordon, 1959) whereas others believed that dividend is irrelevant with the shareholders wealth (Miller and Scholes, 1978) and few argued that dividend and shareholder's wealth are inversely related that is dividend decreases the shareholder's wealth (Litzenberger and Ramaswamy, 1979). The best-known field study in this area is Lintner's path breaking analysis of dividend policy.

Frankfurter and Wood (1997) argue that dividend policy is more of a 'behavioral model'. Some studies have been done to identify the factors that corporate finance managers consider in laying down the dividend policy and it is believed that the findings of the present study will be of use to academia and

practitioners. Dividend payout is considered as one of effective mechanism that can be used by managers to mitigate agency conflicts of interest within the firm for two reasons: First, dividend payout reduces the amount of free cash flow which might be spent by insiders on projects for their own benefits at shareholder expense and second, dividends expose firms to more frequent inspections by the capital markets as dividend payout increase the likelihood of new common stock issue (Easterbrook, 1984).

There are many reasons explaining why dividend policy is so interesting, one of them is that the dividend policy affects its capital structure since the retained earnings intent to fund the firm or otherwise, the firm has to raise funds by issuing new debt.

Consider the case whereby the dividend payment is increased then fewer funds are available internally for financing investments and as a result additional equity capital is needed so the company has to issue new common stock. In real world, firm choose to raise funds instead of retain bigger portion of their earnings because company's dividend decision may change the value of its stock. To date, there is no consensus on what factors affect corporate payout policy. Following Miller and Modigliani's (1961) pioneering dividend irrelevance hypothesis, financial economists have advanced a number of contradicting theories in an attempt to explain why corporate dividend policy does seem to matter in practice. Some have developed around the proposition that dividend policy is relevant due to existence of differential taxes for example, Litzenberger and Ramaswamy, 1979, Poterba and Summers, 1984, and Barclay, 1987) while others argue that clientele effects matter in dividend policy such as Pettit, 1977,

Scholz, 1992 and Allen et al., 2000. Other dividend policy hypothesis suggests that dividend policy is affected by other market imperfections such as information asymmetries and agency costs while the former known as signaling theory predicts that firms can convey information to the market by paying dividends (Bali, 2003). The latter known as agency theory argues that dividends can reduce the costs of shareholder manager conflict (Rozeff, 1982). Debate between these theoretical models remains unresolved and an important observation to emerge from the literature is that once dividend policy is not irrelevant then there are many possible factors that may act as determinant of dividend policy. Importantly also, the literature has concentrated mostly on dividend policy in developed capital markets.

The pattern of corporate payout policies is not only vary over time but also across countries especially between developed and emerging capital market. Glen et al (1995) found that dividend policies in emerging markets differed from those in developed markets and they reported that dividend payout ratios in developing countries were only about two thirds of that in developed countries. Ramcharran (2001) also observed that low dividend yields for emerging market and it was characterized by concentrated ownership and financial systems, such as relying on companies' profits, debts, risks, growth and other factors should be included.

In addition, Aivazian et al (2003) compared a sample of firms operating in eight emerging markets with a sample of 99 US firms. In contrast to Glen et al. and Ramcharran, they observed that payout ratios for emerging market firms were

comparable to their US counterparts and it is worth pointing out that Aivazian et al. used the International Finance Corporation's (IFC) database similar to that used by Glen et al (1995) where only the largest firms were included from each emerging market. Therefore, the paper provide direct test of the impact of ownership structure, such as government and institutional shareholdings on the dividend policy of Indonesia public holding companies. The main objective in this study is to find out all the factors which motivate the dividend decisions and selects topic of "**An analysis of factors influencing the Dividend Policy of Indonesia Stock Exchange listed companies**".

1.2 Research Problems

Based on the background above, the problems of this study are as follows:

1. Is profitability positive significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
2. Is earning variability negative significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
3. Is firm size positive significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
4. Is leverage negative significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
5. Is growth negative significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?

6. Is government shareholdings positive significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
7. Is institutional shareholdings positive significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
8. Is asset structure positive significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?
9. Is firm's age positive significantly affects dividend payout ratio in Indonesia Stock Exchange listed companies?

1.3 Objectives and Benefits Research

1.3.1 Objectives of Research

The purpose of this study is:

1. To determine whether the profitability has positively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
2. To determine whether the earning variability has negatively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
3. To determine whether the firm size has positively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
4. To determine whether the leverage has negatively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.

5. To determine whether the growth has negatively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
6. To determine whether the government shareholdings has positively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
7. To determine whether the institutional shareholdings has positively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
8. To determine whether the asset structure has positively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.
9. To determine whether the firm's age has positively significant affected dividend payout ratio of the listed companies in Indonesia Stock Exchange.

1.3.2 Benefits of Research

Benefits of this research are:

1. Company

Results are expected to provide information to companies regarding the factors that affect dividend policy. The results of this study can be applied by companies in leading to maximize the performance of dividend policy.

2. Investor

The outcome is able to provide an overview of the factors affecting the dividend that currently occurs so that investors are able to do a more accurately in analysis of the business of investing before starting a new investment.

3. Academics

Used as reference for further research and studies especially for the research on effecting the entire companies' performance.

1.4 Systematic Discussions

To facilitate further discussion, the systematic discussion is organized as follows:

CHAP I : INTRODUCTION

This chapter comprises of background research, the formulation of research problems, objectives and benefits of the research, as well as systematic discussion of this research.

CHAP II : THEORETICAL FRAMEWORK FORMULATION & HYPOTHESIS

This chapter contains the supporting previous research topics, literature, theoretical frame work, an explanation of the research that has been done before as well as the basic model of research. Advanced section of this chapter is the formulation of the research hypothesis.

CHAP III : RESEARCH METHODOLOGY

This chapter consists of the approach used in the study, ranging from research outline, research subject, the operational definition of the variables used and data collection techniques. This chapter also discusses the data analysis methods used in the study, which consisted of descriptive statistical analysis, outlier test, classical assumption that consist of multi-colonierity test, auto correlation test, and normality test as well as hypotheses testing.

CHAP IV : DISCUSSION AND ANALYSIS

This chapter describes the analysis of the collected data processing research through statistical testing tools and will be listed the results of the analysis.

CHAP V : CONCLUSIONS, RECOMMENDATIONS AND ITS LIMITATION

This chapter contains the conclusion of the study, limitations of the study and recommendations can be given for future research.