

Moderator Effect of Corporate Governance on the Relationship of Financial Performance and Dividend Policy, and Its Impact on Firm Value in Indonesia Stock Exchange

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Abstract

This study focused on the investigation of moderating corporate governance and financial performance in relation dividend policy and its impact on the firm value in Indonesia Stock Exchange. This study used a survey with an explanatory approach method Moderated Regression Analysis (MRA) and 2 SLS with panel data. The method of estimation uses the Generalized Least Squares (GLS). This study uses secondary data manufacturing companies listed in Indonesia Stock Exchange, for the period of observation from 2006 until 2015. This study resulted in five empirical findings. First, a significant effect on the financial performance of dividend policy, second, corporate governance generally cannot moderate the relationship of financial performance and development policy dividends. Third, the financial performance of a significant effect on firm value, Fourth, corporate governance generally cannot moderate the relationship the firm value and the company's financial performance. Fifth, the dividend policy has no significant effect on firm value. Sixth, dividend policy cannot mediate the relationship financial performance with the firm value.

Keywords: Financial performance; Corporate governance; Dividend policy; Firm value

Introduction

Research background

Until the last three months of 2015, large and medium manufacturing industries had positive work performance in which in October and November, both recorded 10,04% and 0,01% for its performances. However, in November 2015 the industries went downfall and had a weakening of 3.26%. In the midst of development of the manufacturing sector, BPS noted that there are many industries that experienced production decline from January to December 2015.

The issue of corporate governance revived its popularity after few of corporations in U.S such as Goldman Sachs, Bear Stern, Morgan Stanley, Merrill Lynch and Lehman Brothers collapsed. The phenomenon reminded about the beginning of the rise of corporate governance. As the U.S is one of the countries that have high index of CGPI (*Corporate Governance Perception Index*), it raises question on to what extent is the role of corporate governance in supporting the corporations' objectives.

Corporate governance can be used as moderation variable in a research on the relationship between financial performance with dividend policy and the firm value because the firm will be able to maximize its value when it pays attention to its stakeholders or investors. The balance in the achievement of stakeholders' objectives creates opportunity to gain optimal profit and in return the firm's performance will be valued well by the investors.

The well implementation and management of corporate governance or known as good corporate governance is a concept that emphasizes on the importance of the rights of the investors to acquire information correctly, accurately and on time. It also shows the responsibility of the firm to disclose all the information regarding financial performance accurately, transparent and on time. Therefore, both the public firm and private firm must see good corporate governance (CGC) not only as accessories but also as an effort to increase the firm's value. Based on the empirical gap phenomena and the theoretical gap explained

above, the researcher is interested in conducting a research entitled "Moderator Effect of Corporate Governance on the Relationship between Financial Performance and Dividend Policy, and Its Impact on Firm Value in Indonesia Stock Exchange"

Literature Review

There are many researches that explain the negative consequences of weak governance system and attempted to identify the determinant factors that may increase the implementation of corporate governance. Iskander and Chamlou [1], Alijoyo et al. [2] stated that the economic crisis in Southeast Asia and other countries occurred not only due to macroeconomic factor but also due to the weak corporate governance in those countries such as weak laws, weak accounting standards and auditing, under-regulated stock exchange market, weak supervision of commissioners and neglected minority rights.

The measurement of corporate governance practice in the firm level led to many studies that managed to find positive relationship between corporate governance and firm value [3-5]. These studies indirectly showed the usefulness of corporate governance practice in firm level that has been practiced in many countries including Indonesia.

According Berghe and Ridder in their research, to see the relationship between good governance and firm value is not easy. Many previous researches showed that there is no relationship between corporate governance and firm value such as the research of Daily

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and Dalton [6]. The same result was also acquired by Young [7] that analyzed few researches that link corporate governance with firm value.

Klein [8] found that the independent board of directors is more effective in conducting supervision. This was also stated by Cornett et al. [9] where the firm value will increase with the increase of independent commissioners.

Meanwhile Chen et al. [10] also found that the characteristic of independent board, number of meetings and length of service of board have relations with the level of fraud in a firm. Liu and Hu [11] stated that board structure not only serves as control mechanism in the making of finance report but also as controlling shareholder in conducting activities that are disadvantage to the investors.

Lipton and Lorsch [12], Jensen [13], Beiner et al. [14] are the ones that concluded that commissioner board are part of corporate governance mechanism. This was backed up by the opinions of Allen and Gale [15] that stated that commissioner board is a part of an important governance mechanism.

The researches on the impact of independent commissioner to firm value are still varied in its results. There are researches that stated the high proportion of independent board have positive relationship with the firm performance [16-18], and is not included as the factor to firm performance [19], and have negative relationship with the performance [20,21].

The influence of the size of the commissioner board to the firm value also has variety of result. The more personnel that become commissioner board can impact to the worsening of firm performance [22].

Other few researchers found that the size of the board have significant negative influence to the profit management. The lesser personnel of the board means the higher fraud because the less number of the board personnel creates possibility for that [23,24].

Regarding the size of director board, several researchers found different results. Eisenberg et al. stated that there are negative relations between the size of the board and the firm performance. While Dalton et al. stated that there are positive relations between the size of the board and the firm value.

According to Kakabadse et al. [25] the difference result of the researches are caused by few things: 1) theoretical perspectives implemented 2) research methodology 3) performance measurement, and 4) different view on the involvement of the board in decision making. Although these researches on the relationship of corporate governance and firm value showed different results, all showed that corporate governance have direct and indirect influence to the firm value.

The major contribution of a research that studies the relationship between corporate governance and firm value was from Yermack [16], Gompers et al. [26] Cremers et al. [27] and Bebchuk et al. [28]. In these researches, it was concluded that good structure of corporate governance impacts to better performance and increased firm value.

An early study by Baysinger and Hoskinson [29] examined the relationship between percentage of independent commissioner board and firm value. They found that firms with much independent external board are better than firms without. Baysinger and Hoskinson also concluded that the board that consists of the combination of external and internal people from the firm creates the best firm value.

Yermack [16], Bhagat and Black [30], Agrawal and Knoeber [31] found negative correlation between Tobin Q and the proportion of independent board. Bhagat and Black found the relations between the firm values in the market with independent commissioner board. Rosenstein and Wyestt [32] used event study methodology and found small increase of stock price when the firm uses independent board.

Research Purpose

The research purpose is to study on:

- 1) The capacity of finance performance in achieving dividend policy
- 2) How corporate governance moderate the relationship between financial performance with dividend policy
- 3) How financial performance may impact to firm value
- 4) How corporate governance moderate the relationship between financial performance and firm value
- 5) The capacity of dividend policy in achieving firm value
- 6) The capacity of dividend policy in mediating the relationship between financial performance and firm value.

Research Methodology

Methodology

In accordance with the intent and purpose of research as previously stated, the method used in this research is the Explanatory Survey method. This study by its nature is included in descriptive and verificative research [33].

Variable operationalization

Operationalization of variables aims to explain the measurement of various variables and research indicators that are used in this research. They are as follows as shown in Table 1.

Population and Sample

The target population in this study is all manufacturing companies listed on the Indonesia Stock Exchange (BEI), with observation period from 2006 to 2015. From the data acquired from Indonesia Stock Exchange, the number of manufacturing firms from December 2015 is 184 issuers.

The sampling method used in this research is purposive sampling. Purposive method is sampling method in which the researcher has particular criteria and purpose to the samples studied. Based on the data acquired from ICMD from 2006 to 2015, there are only 92 firms that are recorded in Indonesia Stock Exchange.

Analysis design and hypothesis testing

Hypothesis testing on the dividend policy model and firm value is conducted by estimating the following equation:

$$\text{Dividend}_{1it} = a_0 + a_1 \text{ROE}_{it} + a_2 \text{CR}_{it} + a_3 \text{DER}_{it} + a_4 \text{Log(Sale)}_{it} + a_5 \text{FAge}_{it} + \epsilon_{1it} \quad (1)$$

$$\text{Dividend}_{2it} = b_0 + b_1 \text{ROE}_{it} + b_2 \text{KIND}_{it} + b_3 \text{DIR}_{it} + b_4 \text{TT}_{it} + b_5 \text{ROE}_{it} * \text{KIND}_{it} + b_6 \text{ROE}_{it} * \text{DIR}_{it} + b_7 \text{ROE}_{it} * \text{TT}_{it} + \epsilon_{2it} \quad (2a)$$

$$\text{Dividend}_{3it} = c_0 + c_1 \text{CR}_{it} + c_2 \text{KIND}_{it} + c_3 \text{DIR}_{it} + c_4 \text{TT}_{it} + c_5 \text{CR}_{it} * \text{KIND}_{it} + c_6 \text{CR}_{it} * \text{DIR}_{it} + c_7 \text{CR}_{it} * \text{TT}_{it} + \epsilon_{3it} \quad (2b)$$

Variable	Dimension	Indicator	Scale
Endogen	Firm Value (FV)	Tobins Ratio (TBNSQ)	Ratio
Eksogen	Financial Performance (KK)	Profitability: Return on Equity (ROE)	Ratio
		Liquidity: Cash Ratio (CR)	Ratio
		Solvency: Debt to Equity Ratio (DER)	Ratio
Mediation	Dividend Policy (DP)	Dividend Payout Ratio (DPR)	Ratio
Moderating	Corporate Governance (CG)	Composition of Independent Commissioners (KIND)	Ratio
		Directors Board Size (DIR)	Ratio
		Duality (TT)	Ratio
Control	Firm size	Total Asset (TA)	Ratio
	Sale	Sale (Sale)	Ratio
	Firm Age	Listing (Fage)	Ratio

Table 1: Operational definition and research variable measurement.

Sample	Minimum	Maximum	Mean	Standard deviation (n-1)	Skewness (Pearson)	Kurtosis (Pearson)
ROE	(0,3249)	0,5763	0,1202	0,2232	0,109	0,011
CR	0,0003	10462	0,3052	0,3572	1179	-0,101
DER	-19199	39815	13435	14521	0,320	-0,121
KIND	0,1000	0,5450	0,3796	0,0826	0,357	-0,525
DIR	20000	90000	48130	19149	0,835	-0,385
TT	0,0000	0,8000	0,2081	0,2585	1049	-0,032
TA (Juta)	13.173	182.374.000	4.225.641	12.676.756	74147	752336
Sale (Juta)	1	188.053.000	4.226.884	12.678.358	82818	918905
FAGE (Thn)	2	35	154228	53597	0,251	0,160
DPR	0,0000	0,5783	0,1116	0,1744	1282	0,203
FV	(0,3123)	19867	0,9352	0,5913	0,555	-0,713

Source: Result of data processing.

Table 2: Descriptive statistic of research variable.

$$Dividend_{it} = d_0 + d_1 DER_{it} + d_2 KIND_{it} + d_3 DIR_{it} + d_4 TT_{it} + d_5 DER_{it} * KIND_{it} + d_6 DER_{it} * DIR_{it} + d_7 DER_{it} * TT_{it} + \epsilon_{4it} \quad (2.c)$$

$$FV_{it} = e_0 + e_1 ROE_{it} + e_2 CR_{it} + e_3 DER_{it} + e_4 LogTA_{it} + e_5 FAge_{it} + \epsilon_{5it} \quad (3)$$

$$FV_{it} = f_0 + f_1 ROE_{it} + f_2 KIND_{it} + f_3 DIR_{it} + f_4 TT_{it} + f_5 ROE_{it} * KIND_{it} + f_6 ROE_{it} * DIR_{it} + f_7 ROE_{it} * TT_{it} + \epsilon_{6it} \quad (4.a)$$

$$FV_{it} = g_0 + g_1 CR_{it} + g_2 KIND_{it} + g_3 DIR_{it} + g_4 TT_{it} + g_5 CR_{it} * KIND_{it} + g_6 CR_{it} * DIR_{it} + g_7 CR_{it} * TT_{it} + \epsilon_{7it} \quad (4.b)$$

$$FV_{it} = h_0 + h_1 DER_{it} + h_2 KIND_{it} + h_3 DIR_{it} + h_4 TT_{it} + h_5 DER_{it} * KIND_{it} + h_6 DER_{it} * DIR_{it} + h_7 DER_{it} * TT_{it} + \epsilon_{8it} \quad (4.c)$$

$$FV_{it} = i_0 + i_1 Dividend_{it} + i_2 Log(TA)_{it} + i_3 FAGE_{it} + \epsilon_{9it} \quad (5)$$

$$FV_{it} = p_0 + p_1 Pred_DPR_{it} + \epsilon_{11it} \quad (6)$$

Research Result and Discussion

Research variable description

Descriptive statistic is a data description of each variable by using 92 firm samples for 10 years from 2006 to 2015 just as showed in Table 2 below.

The descriptive statistic result above shows that there are four indicators where the average value is above the deviation standard which is KIND, DIR, FAge and FV whereas seven other indicators have bigger deviation standard value than the average.

Hausman test

The test used to determine whether to use Fixed Effect Model or Random Effect Model is Hausman test. The result of the Hausman test is shown in the Table 3 below:

The test result showed that there are 8 equation models that use fixed Effect Model, the result is based on the significant value (p-value) of dividend policy model that is less than 0,05. Meanwhile there is 1 equation model that uses Random Effect Model which is estimation 2c and 6 models.

Test of dividend policy and firm value hypothesis

The empirical model of the estimation result of dividend policy on manufacturing industries recorded in Indonesia Stock Exchange can be seen in the Table 4 below:

Because $F_{hitung} > F_{tabel} (2.2236)$ and $p\text{-value} < \alpha = 0,05$, it can be inferred

	No	Model	X ² -hitung	p-value	Keterangan
Dividend	1	Estimation 1	255262	0,0001	Fixed Effect
	2	Estimation 2.a	242463	0,0010	Fixed Effect
	3	Estimation 2.b	186684	0,0093	Fixed Effect
	4	Estimation 2.c	111033	0,1342	Random Effect
Firm Value	5	Estimation 3	354678	0,0000	Fixed Effect
	6	Estimation 4.a	194751	0,0068	Fixed Effect
	7	Estimation 4.b	234212	0,0014	Fixed Effect
	8	Estimation 4.c	210335	0,0037	Fixed Effect
	9	Estimation 5	189592	0,0003	Fixed Effect
	10	Estimation 6	0,8921	0,3349	Random Effect

Source: Data processing result.

Table 3: Test result of the use of fixed effect or random effect dividend policy model and firm value.

Variable	Expected sign	Equation				Hypothesis Support
		1	2a	2b	2c	
Constant		0,1097*	0,3739*	0,3777*	-0,0576	
ROE	(+)	0,0018**	-0,0218			Yes and no
CR	(+)	0,3529*		-0,0003		
DER	(-)	-0,0046*			0,0463	
KIND	(+)		0,0397**	0,0212*	0,6423*	Yes and no
DIR	(+)		-0,0007	-0,0005	0,0669*	
TT	(-)		-0,0206	-0,0090*	-0,2482**	
ROE × KIND	(+)		0,0371			Yes and no
ROE × DIR	(+)		0,0068*			
ROE × TT	(-)		-0,0124***			
CR × KIND	(+)			-0,0071		No
CR × DIR	(+)			0,0011		
CR × TT	(-)			0,0057		
DER × KIND	(+)				-0,0553	Yes and no
DER × DIR	(+)				-0,0163*	
DER × TT	(-)				0,0065	
Log (Sale)	(+)	0,0170*				Yes
Fage	(+)	0,0022*				
F-stat		1990443	1246306	3681772	69497	Yes
Adjusted R ²		0,9539	0,9925	0,9974	0,0433	

Keterangan: ROE is profitability; CR is liquidity; DER is solvency; KIND is independent commissioners; DIR is the number of directors; TT is duality; Log (Sale) issale; Fage is listing year.

*Statistically supported in alpha 1%

**Statistically supported in alpha 5%,

***Statistically supported in alpha 10%.

Table 4: Test result of dividend policy hypothesis.

that exogenous variable in the model can describe the linear relationship with endogen variable or in other words, the exogenous collectively have significant influence to the dividend value in manufacturing industry listed in Indonesia's Stock Exchange (BEI).

The empirical model of estimation result of company value model at manufacturing industry listed on BEI can be seen in Table 5 as follows:

Information: ROE is profitability; CR is liquidity; DER is solvency; KIND is independent commissioners; DIR is the number of directors; TT is duality; DPR is dividend policy; Pred_DPR: Predicted dividend policy; Log (TA) is the size of the firm; Fage is listing age.

Since $F_{count} > F_{table}$ (2.2236) and $p\text{-value} < \alpha = 0.05$, it can be concluded that the exogenous variable involved in the model can describe the linear relationship with the endogenous variable or in other words the five exogenous variables collectively have a significant effect on firm value on manufacturing industry is listed on BEI.

Research discussion

Dividend policy discussion: The results of this study make it clear that larger companies and the ability to perform financial performances are more likely to pay dividends, as firms with large investment opportunities are less likely to pay dividends. These results are in line with the results of De Angelo and De Angelo [34], Pruitt and Gitman [35], De Angelo and Skinner [36], Baker and Powell, Fama and French [37], Al-Malkawi [38].

The results of this study indicate that independent commissioners as one of the proxies of internal corporate governance structure are less effective in fighting for shareholder rights in the form of dividend payout by the company. The results of this study do not support the findings of Kowalewski, et al. [39] yang presenting that dividend payouts determined by independent commissioners as one of the strengths of internal corporate governance.

The number of directors is able to moderate the performance

Variable	Exp	Equation						Supported by Hypothesis
		3	4a	4b	4c	5	6	
Constant		1,5851*	0,7739*	0,7947*	0,6103*	1,7368*	0,7011*	Yes
ROE	(+)	0,0063**	-0,1016					Yes and no
CR	(+)	0,0635**		-0,5028*				
DER	(-)	-0,0176*			0,0618**			
KIND	(+)		0,2610**	0,0789	0,4624*			Yes and no
DIR	(+)		-0,0194***	-0,0073*	0,0054			
TT	(-)		0,6464*	0,8606*	0,7440*			
ROE × KIND	(+)		0,2425					Yes and No
ROE × DIR	(+)		0,0371**					
ROE × TT	(-)		-0,1655***					
CR × KIND	(+)			0,5829*				Yes
CR × DIR	(+)			0,0283*				
CR × TT	(-)			0,1543*				
DER × KIND	(+)				-0,1016			No
DER × DIR	(+)				-0,0119			
DER × TT	(-)				0,0524			
DPR	(+)					0,0277		No
PRED_DPR	(+)						0,6084*	Yes
Log (TA)	(+)	0,0575*				0,0730*		Yes
Fage	(+)	0,0115*				0,0126*		
F-stat		1817311	3802910	1015,18	6004324	305819	180084	Yes
Adjusted R ²		0,9496	0,9758	0,9908	0,9845	0,9689	0,2528	

Keterangan: ROE is profitability; CR is liquidity; DER is solvency; KIND is independent commissioners; DIR is the number of directors; TT is duality; Log (Sale) issale; Fage is listing year.

*Statistically supported in alpha 1%

**Statistically supported in alpha 5%,

***Statistically supported in alpha 10%.

Table 5: Hypothesis firm value testing result.

relationship with dividend policy. The implication of this research is that the bigger the board of directors the better the company's financial performance in influencing the dividend policy. This means that the addition of one person to the board of directors can lead to effective and efficient decision-making in a company. This study is in accordance with directors positively influence the relationship between financial performances with dividend policy.

In general it can be argued that the duality of the board's role in a manufacturing company can moderate the relationship between financial performance and dividend policy, whereas ideal if there is a duality of roles, the degree of dividend policy will be higher, this is because they can run multiple roles, as supervisors and simultaneously as the executor.

Firm value discussion: The results of this study explain that larger companies and have the ability of financial performance is more likely to value the company, while companies with poor financial performance conditions is less likely to increase the value of the company.

The proportion of independent board of commissioners has no significant effect on the value of the company. The explanation can be given that the addition of independent board members is possible only to meet formal requirements, while majority shareholders (controllers/founders) still play an important role so that the performance of the board does not increase.

Other results also explain that the addition of one person to the board of directors can lead to effective and efficient decision-making within a company. Because, with many members on the board of directors impact on the number of thoughts and suggestions provided

so it will be able to provide meaningful input. This study contradicts Yermack's research [16]; Eisenberg, et al. [22]; Alonso, Palenzuela and Iturriaga stating that directors negatively affect the value of the company.

The results of this study also explain that duality cannot moderate the relationship between financial performances with firm value. These results differ from Saleh et al. research [40] indicates that companies in which there is a duality of role has a positive effect on earnings management. While Klein found that directors with powers exceeding the board of commissioners have the potential to manipulate earnings easily.

In line with the theory put forward by Miller and Modigliani who argue that dividend policy does not affect the value of the company because according to them dividend payout ratio is only the details and no affect the welfare of shareholders [41].

This shows that the company's dividend policy cannot mediate the relationship between financial performance and firm value. The result of earnings regression coefficient, liquidity and solvency in previous equation model 3, yields significant coefficients. The existence of dividend policy no can improve the ability of financial performance to increase the value of the company in the eyes of investors [42-46].

Conclusion and Recommendations

This study yields six conclusions, as follows: 1) High profitability and liquidity can improve the company dividend policy; on the other hand low solvency can improve the company dividend policy. 2) Financial Performance can improve the policy of dividend in the company that enhances the role of director. Conversely, financial

performance can't improve dividend-sharing policies in companies that increase the number of independent and dual commissioners. 3) High profitability and liquidity can increase the value of the company; otherwise low solvency can increase company value. 4) Financial performance can increase the value of a company to a company that enhances the director's role. Conversely, financial performance can't increase the value of the company in the company that increases the number of independent and dual commissioners. 5) A large dividend payout policy can't increase the value of the company. 6) Variable financial performance can't increase the value of the company, through improvement of corporate dividend policy.

Academic Suggestions are; 1) to researchers who will conduct research relevant to this research to include macroeconomic variables in addition to fundamental variables. 2) Subsequent research divides the manufacturing sector into three categories namely basic chemical industry, various industries and consumer goods industry. Practical suggestions are: 1) Investors in taking investment decisions to assess the prospects of future value of the company in addition to consideration of corporate profits

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