The Relationship between Corporate Governance and Dividend Payouts: Evidence from Thai Listed Companies

Received	18/04/2560
Revised	21/08/2560
Accepted	05/05/2560

Sukritta Burinwattana[1] Jantima Ngankokkruad[2]
Chittichai Horthong[3]

Abstract

This research examined the relationship of corporate governance practices and dividend payouts in the Stock Exchange of Thailand (SET). The study used multiple linear regression to examine the effects of several corporate governance factors (board size, CEO duality, audit committee meeting frequency, institutional ownership and CEO compensation policy) on dividend payout ratios in a cross-sectional sample of firms listed on the SET in 2015 (n = 267). The results showed that there was a weak but significant relationship (r2 = 0.246) between institutional ownership and CEO compensation. Other factors were not significant to dividend payouts. The implication of these findings is that while corporate governance practices influence dividend payouts, this effect is weak enough that there are probably additional confounding variables. The relationship between specific corporate governance practices and dividend payouts is not well understood and is an area that requires further study. However, it must be acknowledged that the two factors identified are those that directly relate to the interests of managers and institutional investors. Thus, it is possible that Thailand's public firms have opposing pressures of investor interest, insider self-dealing, and self-interested CEOs and managers.

Keywords : corporate governance, dividend payouts, CEO compensation, institutional interest, Stock Exchange of Thailand

[1] Nakhonratchasima Rajabhat University
e-mail : supa_burin@yahoo.com

[2] Assistant Professor, Nakhonratchasima Rajabhat University

[3] Assistant Professor, Nakhonratchasima Rajabhat University

1. Introduction

This research examined the relationship between corporate governance practices and dividend payouts of companies listed in the Stock Exchange of Thailand (SET). Under agency theory, corporate governance practices are alignment and monitoring costs for the principals (owners) of the firm to ensure that the firm's managers (agents) meet their fiduciary obligations (Mallin, 2016; Jensen & Meckling, 1976, pp. 305-360). Corporate governance can be viewed as a moral obligation in management to the firm and broader society (Sison, 2008). The obligations of corporate governance are particularly important for publicly listed firms, where the economic owners of the firm have little or no control over the firm's management (Tricker, 2015). The SET, the only public exchange in Thailand, first implemented principles of corporate governance for public firms in 2002, after it became clear during the 1997 financial crisis that many firms had taken excessive risk and had not met their governance obligations (The World Bank, 2013). These principles, which were most recently updated in 2012, are designed to be consistent with standards for investor and stakeholder protection and are implemented on a 'comply or explain' basis for publicly listed firms (Stock Exchange of Thailand, 2012). Key areas of concern within the Principles of Good Corporate Governance (GCG) include the rights of shareholders; the equitable treatment of shareholders; the role of stakeholders; disclosure and transparency; and the responsibilities of the board (Stock Exchange of Thailand, 2012). The World Bank (2013) has found that these principles are generally in line with global best practices for corporate governance. Thus, it can be established that there are strong corporate governance principles in place in Thailand. What is less clear is whether these principles influence investor outcomes such as stock performance or dividend payouts. There is ample evidence from other markets that these factors have an influence, which is discussed below, but no such research has been performed in Thailand.

2. Objective of the study

The objectives of the study were to identify required corporate governance practices as a condition of listing on the SET and examine their relationships to dividend payouts in the hope of filling the gap in the literature on corporate governance practices in Thailand and providing more evidence for global corporate governance effects.

3. Literature review and contruction of the study hypothesis

Institutional ownership and dividend payout

Institutional ownership is a key indicator of ownership structure. Findings regarding ownership structure have been mixed depending on countries. One study found that in Egypt, institutional shareholding had a positive and significant relationship to the dividend payout ratio (Abdelsalam, El-Masry, & Elsegini, 2008, pp. 953-964). This finding was similar to the findings of another study in Kenya and Ghana (Abor & Fiador, 2013, pp. 201-225). However, Abor and Fiador (2013, pp. 201-225) did not find a positive relationship in Nigeria, where the effect was negative. Another study in Ghana found an insignificant relationship (Amidu & Abor, 2006, pp. 136-145). Thus, while it is clear that there is a relationship between institutional ownership and dividend payout, the direction is not clear. Therefore, the first hypothesis of this study is that the institutional ownership has a significant effect on dividend payout.

CEO compensation and dividend payout

Next, the effect of CEO compensation, particularly at-risk compensation, was examined. Executive compensation can be considered as two distinct aspects, which are non-risk compensation (fixed salary and benefits) and at-risk compensation (bonuses, stock options, and stock grants) (Mallin, 2016). Several previous studies linked CEO at-risk or share-based compensation and dividend payouts (Brown, Liang, & Weisbenner, 2007, pp. 1935-1965; Minnick & Rosenthal, 2014, pp. 435-454; Sirmans & Ghosh, 2006, pp. 327-355). These studies strongly supported a positive relationship between CEO compensation and dividend payouts and found that firms with higher share-based compensation had higher dividend payout ratios. There are specific conditions that contribute to this relationship. For example, firms where managers are allowed to manipulate dividend policies may see a rise in dividends as a means of stealth compensation (Minnick & Rosenthal, 2014, pp. 435-454). Brown, Liang and Weisbenner (2007, pp. 1935-1965) also found that the relationship was stronger under favorable tax conditions. Thus, among all the corporate governance factors examined here, CEO at-risk compensation can most easily be predicted in terms of significance and direction. Therefore, it was hypothesized that the CEO at-risk compensation has a significant positive effect on dividend payout.

Board size and dividend payout

Board size was hypothesized to have a negative effect on firm outcomes, because larger boards can create social norms and pressures that discourage effective oversight (Cornett,

McNutt, & Tehranian, 2009, pp. 412-430). However, studies on board size and dividend policy have had mixed findings. One study did not find board size to have a significant effect on dividend payouts (Abdelsalam, El-Masry, & Elsegini, 2008, pp. 953-964). However, two other studies found a positive and significant relationship between board size and dividend policy. (Abor & Fiador, 2013, pp. 201-225; González, Guzmán, Pombo, & Trujillo, 2014, pp. 365-385). Abor and Fiador (2013, pp. 201-225) compared data from three countries and found a negative relationship in one country. Overall, the evidence supported a significant relationship of board size and dividend payouts, although the direction may vary. Therefore, the third hypothesis is that the board size has a significant effect on dividend payout.

Audit committee meeting frequency

Audit committee quality and its effect on dividend payout has been studied using a number of different dimensions (Jiraporn, Kim, & Kim, 2011, pp. 251-279; Nimer, Warrad, & Khuraisat, 2012, pp. 172-179; Sawicki, 2009, pp. 211-230). Authors took different approaches, including generation of an audit committee quality index (Jiraporn, *et al.,* 2011, pp. 251-279; Sawicki, 2009, pp. 211-230) and use of individual characteristics (Sawicki, 2009, pp. 211-230). The bulk of evidence supported a positive relationship between audit committee quality, including dimensions of audit committee meeting frequency (Jiraporn, *et al.,* 2011, pp. 251-279; Sawicki, 2009, pp. 211-230). For this study, only audit committee meeting frequency could be studied, because the Form 56-1 information available has minimal and inconsistent disclosures about audit committee quality. Thus, the fourth hypothesis of this study is that the audit committee meeting frequency has a significant effect on dividend payout.

CEO duality and dividend payout

Several studies have addressed CEO duality and its effect on dividend policy (Abdelsalam, et al., 2008, pp. 953-964; Abor & Fiador, 2013, pp. 201-225; González, *et al.,* 2014, pp. 365-385; Sirmans & Ghosh, 2006, pp. 327-355). Directionality of these relationships has been mixed. While some studies found a negative relationship (Abor & Fiador, 2013, pp. 201-225; Sirmans & Ghosh, 2006, pp. 327-355), others found a positive relationship (González, *et al.,* 2014, pp. 365-385). Abdelsalam, *et al.* (2008, pp. 953-964) did not find it significant at all, while two out of three countries surveyed by Abor and Fiador (2013, pp. 201-225) did not have a significant relationship. This suggests that the effects are country-specific. Since the expected relationship in Thailand is not known, it was hypothesized that the CEO duality has a significant effect on dividend payout.

4. Research Methods

4.1 Sample and data collection

The population included in this study was non-financial and non-property firms listed on the SET in the year 2015. Financial and property firms were excluded because of differences in their financial management practicing and reporting (Gibson, 2009). Out of 497 firms listed on the SET, 58 were financial firms and 13 were property and construction firms (SET, 2016), which reduced the population to 426 firms. A further 159 firms were excluded because of incomplete information about dividend payments or CEO compensation, or because they were under rehabilitation. The final sample was n = 267 firms. Data were collected from the SETSMART database, which provided access to all publicly listed firm information included in the mandatory, annual Form 56-1 filing.

4.2 The measurement characteristics of the variable

Table 1 Definition and operationalization of variables

Variable	Abbreviation	Measurement
Institutional Ownership	INSTOWN	Percent of shares owned by institutional investors.
CEO Compensation	CEOCOM	Price-sensitive compensation assigned to CEO. *Log (CEOCOM)*
Board Size	BSIZE	Number of board members. *LOG (BSIZE)*
Audit Committee Meeting	AUMEET	Number of audit committee meetings *LOG (AUMEET)*
CEO Duality	CEODUO	Dummy variable : 0 : Dual CEO 1 : Non-Dual CEO
Dividend Payout Ratio	DIV	Dividend paid/Net profit
Control variables	AGE	Years since firm listed on SET *Log (AGE)*
	BIG4	The firm uses a Big 4 auditor Dummy variable : 0 = no, 1 = yes
	Industy	Industry the firm participates in Dummy variable : 0 = services, 1 = industry

5. Results

5.1 Descriptive statistics analysis

Descriptive statistics shown in Table 2 includes minimum, maximum, mean and standard deviation calculated for the study variables. DIV is between a minimum of 0.03 and a maximum of 373.51 with an average of 2.08. INSTOWN falls in the ranged from 0% to 94.06%, with a mean of 23.65%. CEOCOMP ranged from 3.20 to 449.72, with a mean of 52.70 while LOGCEOCOM ranged from 0.51 to 4.68 (M = 1.314). BSIZE ranged from 6 to 21 members, with an average of 11 members. AUMEET ranged from 1 to 25, with a mean of 6.04 a year. LOGAUMEET ranged from 0.30 to 1.40 (M = 0.74, SD = 0.18). CEODUO ranged from 0 to 1, with a mean of 0.73.

Table 2 Independent and dependent variables used of Descriptive statistics analysis

	N	Minimum	Maximum	Mean	Std.Deviation
INSTOWN	267	.00	94.06	23.65	23.381
CEOCOM	267	3.20	449.72	52.70	64.422
LOGCEOCOM	267	.51	4.68	1.31	.464
BSIZE	267	6	21	11.00	2.730
AUMEET	267	1	25	6.04	3.496
LOGAUMEET	267	.30	1.40	.74	.183
CEODUO	267	0	1	.73	.447
DIV	267	.03	373.51	2.08	22.832
AGE	267	1	40	18.25	9.560
LOGAGE	267	.00	1.60	1.16	.371
BIG4	267	0	1	.71	.456
INDUSTY	267	0	1	.77	.421

The regression analysis examined predictor variables (INSTOWN, LOGCEOCOM, BSIZE, LOGAUMEET, CEODUO, LOGAGE, BIG4, and INDUSTY) against the outcome variable DIV. The model's goodness of fit is only moderate (r2 = .246), indicating that 24.6% of the variance in DIV can be predicted from variance in the predictor variables. This is a relatively weak regression equation (r2 < .300) (Hair, Anderson, Black, & Babin, 2016). According to the t-tests,

only two predictors were significant, including INSTOWN ($p = .012$) and LOGCEOCOM ($p < .001$). Thus, H1 and H2 can be accepted, as INSTOWN (negative) and LOGCEOCOM (positive) had significant relationships to DIV. however, H3, H4, and H5 must be rejected, as the relationships of BSIZE, LOGAUMEET, and CEODUO were not significant.

5.2 Discussion

Testing of the hypotheses showed that while institutional ownership (INSTOWN) and CEO compensation (LOGCEOCOM) had significant effects on dividend payout (DIV), the three board structure variables – board size (BSIZE), audit committee meeting frequency (LOGAUMEET), and CEO duality (CEODUO) – did not have significant effects. The reasons for some of these relationships are clear, but others are less clear.

Institutional ownership had a negative effect on dividend payout. This finding is most consistent with Abor and Fiador's (2013, pp. 201-225) finding in Nigeria, which was the only situation in which a negative relationship was observed. Other studies that were reviewed had a positive effect. As Abor and Fiador (2013, pp. 201-225) noted, effects of institutional ownership varies widely in its extent and effects depending on the country, and different institutional frameworks influence the role of institutional ownership as well. Institutional ownership in different countries may also have different levels of activity; for example, in Kenya it is known that institutional investors are mainly inactive foreign portfolio investors (Abor & Fiador, 2013, pp. 201-225). Institutional ownership was much lower in this study than in countries where institutional ownership was positively associated with dividends (Abdelsalam, et al., 2008, pp. 953-964; Abor & Fiador, 2013, pp. 201-225). Thus, it is an open question as to whether this relationship comes about because of institutional investor inactivity or because of lack of investor influence on firm decisions. This remains an area for furture study in Thailand.

CEO at-risk compensation had a positive effect on dividend payout. This relationship was fully expected, given that previous studies have shown that CEOs with higher levels of at-risk compensation or higher advantages from dividend payments are more likely to manipulate dividend policy to increase dividend payouts (Brown, *et al.,* 2007, pp. 1935-1965; Minnick & Rosenthal, 2014, pp. 435-454). To be clear, it is not proved by this study that CEOs manipulate dividend payout in this case; it is possible, for example, that firms that perform better in the market can both provide higher levels of CEO compensation and higher dividend payouts. Determining whether this is a direct causal chain, or where there are additional

variables that could influence both of these factors and their relationship. However, given the prior evidence provided by Brown, *et al.* (2007, pp. 1935-1965) and Minnick and Rosenthal (2014, pp. 435-454), there is a good reason to examine more thoroughly the conditions under which Thai firms set their dividend payout and what factors influence them, including CEO compensation strategies. Unlike other factors such as institutional ownership, it is possible that the effect of CEO compensation on dividend payout is robust across countries, since it is determined by individual relationships rather than institutional factors. Abor and Fiador's (2013, pp. 201-225) suggested that institutional frameworks may influence some factors differently than others. Although CEO compensation was not included in their study, this could be a useful extension of the research.

Board structure variables did not appear to have a significant effect on dividend payout. There were some preliminary evidences from other countries that the board structure characteristics like board size, audit meeting frequency and CEO duality, would influence dividend payout, but these effects were inconsistent between studies (Abdelsalam, *et al.,* 2008, pp. 953-964; Abor & Fiador, 2013, pp. 201-225; Amidu & Abor, 2006, pp. 136-145; Cornett, *et al.,* 2009, pp. 412-430; González, *et al.,* 2014, pp. 365-385; Jiraporn, *et al.,* 2011, pp. 251-279; Nimer, *et al.,* 2012, pp. 172-175; Sawicki, 2009, pp. 211-230; Sirmans & Ghosh, 2006, pp. 327-355). Since there was such inconsistency in the board structure literature, it is not surprising that these factors were not significant in the current study. It is possible that a more detailed analysis of corporate board structure could identify some impact on dividend payout ratio. However, it is also possible that dividend payouts are mainly determined by the firm management, rather than the corporate board. Since this is not reflected in the Form 56-1, it would require a more extensive evaluation of firm evidence in order to determine whether there is such a relationship.

6. Conclusion and Recommendations

This study examined the effects of different aspects of corporate governance practices on dividend policies of publicly listed firms in Thailand. Dividend policies were measured using the firm's dividend payout ratio. The analysis showed that institutional ownership had a negative effect on the dividend payout ratio, while CEO at-risk compensation had a positive effect. These relationships were somewhat consistent with the literature, although there is a possible institutional and market interaction for institutional investment and dividends.

In contrast, the mechanism for CEO compensation's effect on dividend policy was clear, since previous studies identified self-interested reasons for the relationship such as stealth compensation and taking advantage of positive tax policies. In contrast, board structure had insignificant effects on dividend policy. Although the reason for this is not clear, it is possible that Thai boards have limited influence on setting dividend policies. In conclusion, ownership structure and CEO compensation strategies influence the firm's dividend payouts in Thailand, although board structure appears not to.

There are some limitations to this research that need to be considered. Since the study was cross-sectional, multi-year trends and seasonality effects that could influence dividend payouts were not taken into account. The study was also limited in that it excluded financial and property firms, which could have different patterns than service, manufacturing and other firms. These limitations offer opportunities for further research, for example a time series study of corporate governance that compares pre- and post-Principles of GCG implementation. Further study could also incorporate additional variables, such as a wider perspective on audit committee quality including aspects like number of members, expertise, and outsider board members. This type of extended study could provide more information on the role of corporate governance on the firm's dividend payout ratio. Comparison to other countries could also provide more information about the institutional frameworks, regulatory environment and other market characteristics that influence the relationship of corporate governance and dividend payouts or other investor interest variables, such as earnings quality, information quality or total shareholder returns.

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