Large Shareholders, Payout Policy and Agency Problems in Malaysian Companies

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This study investigates the effect of large shareholders on the magnitude of payout ratio. The analysis revealed that the higher the largest shareholding, the higher the payout ratio of the company. Furthermore, this paper found that the presence of a substantial second largest shareholder has a significant and positive impact on the payout ratio of Malaysian companies. However, different types of the large shareholder have no statistically significant influence on the magnitude of payout ratio. This study enhances the understanding of payout policy based on agency perspectives and provides evidence from an Asian country.

INTRODUCTION

Recent studies have noted that many publicly listed companies located outside the United States (U.S.) and the United Kingdom (U.K.) have high concentration of ownership, wherein a single large shareholder or shareholder group controls a company or corporation (Claessens, Djankov, & Lang, 2000; Faccio & Lang, 2002; La Porta, Lopez-De-Silanes, & Shleifer, 1999). The evidence suggests that the large shareholders in developed countries besides the U.S. and the U.K., European countries and East Asian countries, operate in such a way that they negate the concept of separation of ownership from control discussed by Berle and Means (1932).

Effective control by large shareholders enables them to influence the decisions regarding how companies are run, as well as how their corporate policies are developed and put into practice. However, the role of large shareholders is not well developed in the ownership literature, especially the role of the largest shareholder (Holderness, 2003). The largest shareholder is a unique type of shareholder, where their holding is associated with benefits and costs, especially underinvestment costs (Claessens, Djankov, Fan, & Lang, 2002; Truong & Heaney, 2007). One type of company decision that is generally influenced by corporate ownership structure concerns payout policy. Companies will always need to make decisions on what percentage of earnings that needs to be paid out as dividends, and in what form to distribute cash to shareholders.

It has been suggested that corporate payouts are used to alleviate agency problems (Easterbrook, 1984; Jensen, 1986; Rozeff, 1982). According to agency perspectives, the non-existence of effective governance simply encourages managers to expropriate corporate funds. Managers are free to pursue endeavours that serve their interests and they would not properly devote their time or resources to profitable investments or allocate earnings to shareholders. Distribution of a company's earnings may go no further than the managers, and for this reason corporate payouts have become a corporate governance device to mitigate agency conflicts. Mancinelli and Ozkan (2006) highlight that many studies have been

undertaken previously on the subject of payout policy, yet little research had been done on agency-based-explanations of corporate payouts. As stated by La Porta, Lopez-de-Silanes, Shleifer and Vishny (2000, p. 2), 'the idea of dividend policy in addressing agency problem has been getting limited attention until recently'. Claessens and Fan (2002) even suggest payout policy serves as an alternative governance device in emerging markets as conventional governance instruments are not effective in mitigating or solving agency concerns.

The objective of this paper is to investigate the impact of large shareholders on corporate payout policy, from the perspective of agency arguments. Specifically, listed companies in an emerging economy, Malaysia, are examined. Instead of focusing only on a single payout channel (i.e. dividends) as many studies have done, this study investigates the influence of large shareholders on corporations' total payout distribution (i.e. dividends and share buy-backs). Recent studies on payout policies (e.g. Fama and French 2001; Grullon and Michaely 2002) find that share buy-backs have become an important form of payouts. Fama and French (2001) explain that share repurchase are not substitutes for dividends. Alternatively, due to the tax advantage of share buy-backs in the U.S., Grullon and Michaely (2002) argue that share buy-backs are used as a substitute for dividends.

Malaysia provides an interesting background when examining this issue because its corporate ownership structure is concentrated and large shareholders are in control of a large proportion of listed companies. Tam and Tan (2007) observe that on average, the largest shareholder in Malaysia owns 43 percent of companies' issued capital. Truong and Heaney (2007) also reported that the largest shareholder in Malaysia maintains a relatively substantial ownership interest, with an average largest shareholding of more than 33 percent. Another area of focus in this study concerns how the largest shareholder is classified, i.e. whether they are a family, an institution or the Government. Prior evidence shows that the largest shareholder in European companies is more likely to be a financial institution, whereas a family group is more likely to be the largest shareholder in East Asian companies. The differences in the composition of the ownership structure may also influence the payout policy of companies. It is intended in this study to shed light on this issue by looking at the evidence from Malaysia, which is an emerging market in Asia.

AGENCY THEORY, PAYOUT POLICY AND OWNERSHIP STRUCTURE

According to Jensen and Meckling (1976), agency theory distinguishes the agency relationship between principals and the agent. Problems will arise when shareholders (principals) do not manage the corporation themselves, as managers (agents) are free to pursue activities that serve their own interests instead of the shareholders' interests. Agency theory suggests that large shareholders ownership may either alleviate or exacerbate agency conflicts. The agency problems in a company can be reduced when the level of managerial ownership is high, as managers also have to bear a fraction of the losses that may arise from their opportunistic behaviour (Jensen & Meckling, 1976; Morck, Shleifer, & Vishny, 1988). In addition, large shareholders could also mitigate agency problems because they have a strong motivation to maximize the company's wealth (Shleifer & Vishny, 1997) and have the capabilities in gathering information in monitoring the company (Shleifer & Vishny, 1986). Nevertheless, there is a possibility of expropriation by large shareholders, as their interest may not match the interest of minority shareholders (Shleifer & Vishny, 1997).

Corporate payouts also can be used as a corporate governance (CG) mechanism in reducing agency problems. According to optimal dividend payout/cost minimization model postulated by Rozeff (1982), dividend payments can be part of a corporate monitoring tool. Easterbrook (1984) also views that corporate payouts can mitigate agency concerns by subjecting companies to capital market monitoring. Based on the free cash flow hypothesis, Jensen (1986) suggests that companies' cash can be limited from the hand of managers by distributing higher payouts. Therefore, managers' investment in uneconomic projects or wastage on perquisites can be reduced. The association between the managerial ownership and payout policy has been extensively examine in empirical studies, particularly in the U.S. market such as Agrawal and Jayaraman (1994), Moh'd, Perry and Rimbey (1995) and Rozeff (1982).

Possible agency conflicts between large shareholders and minority shareholders can also be controlled by corporate payouts. A pro-rata distribution can be guaranteed to all shareholders when a company distribute corporate payouts, and thus, limit corporate wealth from large shareholders' control (Gugler, 2003). La Porta et al. (2000) indicate that minority shareholders in countries with stronger legal protection system will use their power to force controlling shareholders to pay higher payouts. Controlling shareholders can also use corporate payouts to compensate the minority shareholders' concern, especially in an environment where expropriation by controlling shareholders exists (Faccio, Lang, & Young, 2001). However, lower fund distributions can be observed in companies with higher existence of large shareholders ownership, as payouts are not needed to act as an alternative agency control mechanism (Goergen, Renneboog, & Correia da Silva, 2005). Payouts become a substitute device to large shareholder ownership in alleviating agency problems, as high level of payout distributions could result in underinvestment risk and unnecessary liquidity constraints. However, lower payouts could also a result of agency conflicts between large controlling shareholders and minority shareholders (Gugler & Yurtoglu, 2003).

The relationship between the largest shareholder and payout policy has been investigated by several studies, especially based on European companies. Gugler and Yurtoglu (2003), Maury and Pajuste (2002), Mancinelli and Ozkan (2006), Renneboog and Szilagyi (2006) and Renneboog and Trojanowski (2007) have examine the association between the largest shareholder and payout policy for companies in Germany, Finland, Italy, Netherland and UK, respectively. They find that the largest shareholder has a negative relationship with the payout policy. However, based on the sample drawn from 37 countries, Truong and Heaney (2007) observe a positive association between the largest shareholder and corporate payouts.

Claessens et al. (1999) analyse the corporate ownership structure of East Asian countries and find that two-thirds of the companies are controlled by a single controlling shareholder. They view that the existence of large controlling shareholders is related to the expropriation of minority shareholders by controlling shareholders. Considering the institutional environment of Asian countries and, based on the expropriation argument, the controlling shareholders in this region are expected to prefer lower payout distributions. This study, therefore, explores whether Gugler and Yurtoglu's (2003) expropriation argument is relevant to East Asian companies, and specifically those that are Malaysian listed companies. Therefore, given the institutional background in Malaysia, the study proposes the following hypothesis:

> *Hypothesis 1: The payout policy of Malaysian companies is negatively related to the ownership interest of the largest shareholder.*

The relationship between the largest controlling shareholder and payouts, however, might not be linear at all levels of ownership holdings. A non-linear relationship between managerial ownership and payout policy has been observed by Schooley and Barney (1994) and Farinha (2003), while a non-linear relationship between the largest shareholder and payout policy was documented by Gugler and Yurtoglu (2003), Correia da Silva, Goergen and Reneboog (2004) and Truong and Heaney (2007). The managers' divergent behaviour can be curbed by the largest shareholder's direct monitoring at a relatively low level of shareholding. Therefore, the efficient monitoring by the largest shareholder will result in higher payouts, and these will limit managers' ability to disgorge available funds. Yet, at a certain level of ownership, the private benefits of control outweigh the earnings return received by the largest controlling shareholder. Therefore, the largest shareholder has a preference for retaining corporate resources and payouts will shrink. In line with the above discussion, the following hypothesis is being tested:

> *Hypothesis 2: The payout policy of Malaysian companies is negatively related to the ownership of the largest shareholder below a specific level of holding, and positively related to the ownership of the largest shareholder beyond that level of holding.*

Recently, accounting and finance researchers also have analyse the effect of other large shareholders, beside the largest one, on companies based from agency perspectives. Prior studies have discussed these effects from two dimensions. In one hand, Bolton and von Thadden (1998) and Pagano and Roell (1998) view that other large shareholders could monitor the controlling shareholder. The monitoring role play by the other large shareholders therefore, could limit the expropriation of minority shareholders' resources. In another hand, Faccio et al. (2001) and Pagono Roell (1998) state that other large shareholders may collude with the controlling shareholder in expropriating corporate resources and share the private benefits (Faccio et al., 2001; Pagano & Roell, 1998). Empirical evidence on the impact of other large shareholders on payout policy has been limited. Faccio et al. (2001) find that the presence of multiple large shareholders in Europe minimizes the expropriation activity of the controlling shareholder, thus resulting in higher dividend payments, while in Asia, lower dividend rates are being observed. They conclude that the controlling shareholder collaborate with other large shareholders to expropriate the minority shareholders in Asia.

This study, therefore, explores whether Faccio et al.'s (2001) conclusions regarding the negative impact of other large shareholders in Asia on payout policy are relevant to Malaysian listed companies, or whether the second largest shareholder mitigates the expropriation activities by the controlling shareholder as suggested by Gugler and Yurtoglu (2003) and thus, have a positive influence on payout policy. This study proposes another hypothesis as follows:

> *Hypothesis 3: The payout policy of Malaysian companies is positively related to the second largest shareholder ownership level, or the existence, of the second largest shareholder.*

The category into which the largest shareholder falls may influence dividend decisions (Gugler & Yurtoglu, 2003). Gugler (2003) views that as large family shareholders have more incentive to monitor the company directly, the function of dividends as a monitoring tool become limited. Ho, Verhoeven and Wu (2008) find that small to medium size family-controlled companies have higher dividend payouts than large family-controlled companies. Gugler (2003) also suggests that agency problems in Government owned companies are more severe than other companies due to the double principal-agent relationship. The author explains that the ultimate owners of Government-owned companies are the citizens, and the citizens have fewer incentives to monitor the companies. Furthermore, the representatives of citizens do not actively monitor the companies, as they are also not strongly monitored by the citizens. Higher payout levels therefore, can be expected in Government-owned companies, as payouts can act as a device to mitigate agency concerns.

Institutional shareholders and payout distributions can be viewed as a substitute in monitoring a company (Zeckhauser & Pound, 1990). Payouts for companies controlled by an institutional investor can be expected to be low as payouts are not required as a governance mechanism. Kouki and Guizana (2009) state that institutional shareholders prefer paying benefits to themselves instead of distribute dividends to all shareholders. However, as a large shareholder with strong monitoring skill, institutional investors would encourage company to distribute higher payouts to avoid being expropriated (Renneboog & Szilagyi, 2006). Institutional investors may also think that their role in monitoring the company is not enough or their efforts are very costly, and thus prefer the company to be monitored by external capital markets (Farinha, 2003). Abdelsalam, El-Masry and Elsegini (2008) also find that companies in Egypt with higher institutional shareholders ownership have a higher dividend payout ratio.

The domestic institutional shareholders in Malaysia, however, are a member of Minority Shareholders Watchdog Group (MSWG), where its establishment is expected to play a significant part in developing institutional shareholder activism in Malaysia. As a member of MSWG, the domestic institutional shareholders are expected to effectively monitor company's decision-making and performance, and, thus, minimize any potential agency conflicts within a company. Therefore, payouts are expected to be smaller in companies owned by an institutional shareholder, as they would substitute

for the monitoring function of payouts. The hypothesis relating to types of the largest shareholder are as follows:

> *Hypothesis 4: The payout policy of Malaysian companies is negatively related to the largest shareholder that is categorized as a family group and institutional shareholder, respectively and positively related the largest shareholder that is categorized as the Government.*

DATA AND METHODOLOGY

This paper focuses on non-financial public listed companies (PLCs) of Bursa Malaysia (Malaysian Stock Exchange) that consistently listed on the Main Board over the period of 2002 to 2006. This study utilised the data from Nathasa Mazna (2010), where a systematic random sampling of one for every two companies in the population is applied. A systematic random sampling is used due to the extent of data required in this thesis, particularly relating to ownership data, as it is unrealistic to analyse the complete population of Malaysian listed companies. Financial, trusts and closed-end funds companies are excluded, as they are subjected to a regulatory framework that does not apply to other listed companies. In addition, companies that were classified under Practice Note 4/2001 during 2002 to 2006 are excluded (distressed companies/companies with negative shareholders' funds). The final sample contains 245 companies, which covers 1,225 firms-years observations.

Sources and Collection of Data

Data related to the ownership of the sample companies are hand-collected from the annual reports, which are downloaded from the website of Bursa Malaysia (http://www.klse.com.my). The collection of ownership data is started with the list of the 30 largest shareholders of each of the listed companies. This study focuses on two categories of large shareholders which are the largest and the second largest shareholder. The largest shareholder is defined as the largest shareholder who owns directly and indirectly the equity of the company. The second largest shareholder is defined as the next largest shareholder who is not affiliated with the largest shareholder. The above disclosed information is generally provided in the analysis of shareholdings section in an annual report. This analysis scrutinizes thoroughly each company's annual reports to collect the relevant information. Extra care is taken to identify the indirect holdings of the largest shareholder.

Extending the work of Nathasa Mazna (2010), this study further classified the largest shareholder into four mutually exclusive groups, namely individual/family, Government, trust funds/institutional investors and a foreigner. The study does not distinguish between family members. The study use the family group as a unit of analysis, as it is assumed that they vote as a coalition. Family includes people that are related through blood or marriage. This study assumes that people with the same surname and people that have the same father's name belong to the same family. For Muslims in Malaysia, their name will include their father's name after the word 'Bin' or 'Binti' which mean 'the son of' or 'the daughter of', respectively.

The largest shareholder is categorized as the Government if it can be categorized as representing one of the following bodies: 1) the Federal Government; 2) the State agencies; and 3) the Federal Government-Linked agencies/Government-Linked Investment Companies (GLICs). The Government-Linked institutional shareholders are classified as an institutional investor, due to its principal activities and characteristics. Trust funds/institutional investors' category include insurance companies, pension funds, professional fund managers and licensed banking institutions. A company with the largest shareholder is a foreign company or foreign individual, is classified as foreigners. For companies which the largest shareholder is a private company, the study looked at the ultimate owner of the private company until the largest shareholder can be classified into one of the above type of the largest shareholder. In order to enhance data accuracy, the type of ownership classification is verified with the classification of ownership from the OSIRIS database.

The main source for financial data is OSIRIS database, except for data related to share buy-backs activity. Apart from that, companies' annual reports and Thomson One Analytical database are used. The main source is confirmed by reference to other sources whenever this is possible to improve accuracy. Data on share-buybacks are obtained manually from the individual company's annual reports.

Model Specifications

The study use random-effects Tobit regressions to analyse the influence of large shareholders on the level of payouts. The model to be estimated can be expressed as:

$$\mathrm{Y_{it}} = \alpha + + \sum_{j=1}^{5} b_j \mathrm{LARGE\,SHAREHOLDERS}_{jit} + \sum_{k=1}^{3} b_k \mathrm{TYPE}_{kit} + + + \sum_{l=1}^{5} b_l \mathrm{CONTROL}_{lit}$$

$$+ \sum_{m=1}^{4} b_m \mathrm{TIME}_{mit} + \sum_{n=1}^{8} b_n \mathrm{INDUSTRY}_{nit} + \mu_{it}$$

(Equation 1)

$$\mathrm{Y}_{it} = \begin{cases} \mathrm{Y}^*_{it} \text{ if } \mathrm{Y}^*_{it} > 0 \\ 0 \text{ if } \mathrm{Y}^*_{it} \leq 0 \end{cases}$$

(Equation 2)

Where:

μ_{it}	:	the unobserved error component
Y^*_{it}	:	Dependent variable, which is the total payout (the sum of total dividends and share buy-backs) divided by earnings ratio (TPE)
LARGE SHAREHOLDERS$_{jit}$	:	set of variables for various classifications of large shareholders: The largest shareholding (LARGEST), LARGEST raised to the power of 2 (SQLARGEST), the second largest shareholding (SECOND), and the existence of a substantial second largest shareholder who owns equal or more than 5 percent of total paid-up capital (SECOND5%)
TYPE$_{kit}$	:	Set of variables either FAMILY, GOVERNMENT or INSTITUTIONAL for k=1,2 or 3 respectively.
CONTROL$_{lit}$	:	set of control variables: profitability (ROA), firm size (SIZE), investment opportunities (INV), debt level (DEBT) and risk level (RISK)
TIME$_{mit}$	:	set of year dummies that, respectively, take a value of 1 for 2003, 2004, 2005 and 2006, or 0 if otherwise
INDUSTRY$_{nit}$	:	Set of industry dummies that, respectively, take a value of 1 for companies categorized in construction, consumer products, industrial products, infrastructure project companies, hotels, plantations, properties and technology, or 0 if otherwise

Details of independent and control variables are explained in Table 1.

TABLE 1
INDEPENDENT AND CONTROL VARIABLES MEASUREMENT

Notation		Explanation
INDEPENDENT VARIABLES		
LARGE SHAREHOLDERS		
LARGEST	:	The proportional holding of the largest shareholder
SQLARGEST	:	LARGEST raised to the power of 2
SECOND	:	The proportional holding of the second largest shareholder
SECOND5%	:	Dummy variable takes the value of 1 if the second largest shareholding is equal or more than 5 percent, 0 if otherwise
TYPES OF THE LARGEST SHAREHOLDER		
FAMILY	:	Dummy variable equal to 1 if the largest shareholder is a family group, 0 if otherwise
GOVERNMENT	:	Dummy variable equal to 1 if the largest shareholder is the Government, 0 if otherwise
INSTITUTIONAL	:	Dummy variable equal to 1 if the largest shareholder is an institutional shareholder, 0 if otherwise
Table 1 continued:		
CONTROL VARIABLES		
ROA	:	is the ratio of earnings before interest and taxes to total assets
SIZE	:	is the natural log of total assets
INV	:	is the ratio of market capitalization to total assets
DEBT	:	is the ratio of the book value of total debt to total assets
RISK	:	is the standard deviation of monthly share returns

RESULTS AND DISCUSSION

Correlations Between the Independent Variables

Bivariate correlations between independent variables are calculated to test for multicollinearity. The correlation matrix reveals that there are a few variables that have high inter-correlation (above 0.5). However, the high inter-correlations are between the large shareholder ownership variables, thus, they do not indicate that multicollinearity is a serious problem for the analysis that will be conducted. This is because these variable combinations will generally not be included together in the same regression model. In addition, as the correlation results are below the critical value limit of 0.90 (Gujarati, 2003), therefore, it can conclude that no multicollinearity problems impacting on the regression analysis have been detected.

Descriptive Statistics

The financial characteristics for the sample of 245 companies for the period 2002-2006 are summarized in Table 2. There is considerable skewness in total assets figures, with the mean and median values of RM1, 772 million and RM467 million respectively. Due to the skewness in total asset levels, the study transforms the value into the natural logarithm of the total assets to use as a proxy for size. The leverage exposure of the companies is moderate, where the average percentage of the total debt over the total assets is 21.8 percent. The mean profitability level, measured by ROA level is 5.40 percent and the median ROA level is 6 percent. The mean and median of the investment opportunities ratio are 0.691 and 0.458, respectively. The average investment opportunities ratio (Tobin's Q) is less than 1.00, and this suggests low growth or poor managerial performance. There is also minimal difference between the mean and median levels of firm risk, which are 0.091 (mean) and 0.079 (median).

TABLE 2
FIRM'S CHARACTERISTICS OF 245 MALAYSIAN LISTED COMPANIES, 2002-2006

Variables	N	Mean	Median	Minimum	Maximum	Standard Deviation
Total assets (RM Mil)	1225	1,772	467	2	65,092	5,458
Total debt/total assets	1225	0.218	0.198	0.000	1.646	0.198
Investment (Tobin's Q)	1225	0.691	0.458	0.024	13.784	0.865
Return on assets	1225	5.40%	6.00%	-129.03%	79.62%	12.20%
Standard deviation of returns (Risk)	1225	0.091	0.079	0.015	0.549	0.058

The distribution of the sample companies' ownership is exhibited in Table 3. The statistics in the table indicate that ownership concentration is high among Malaysian listed companies. The largest shareholder, on average, holds 40.21 percent of the company's total equity holding. This percentage holding is higher than the largest average shareholding as reported by Truong and Heaney (2007) of 33.18 percent for Malaysian companies. The result of this paper, however, is slightly lower than the average largest shareholder ownership of 43 percent as report by Tam and Tan (2007). The second largest shareholder also holds a substantial holding with a mean value of 10.79 percent. The number of companies with a significant second largest shareholding is high, with more than 75 percent of the sample firm observations having a second largest shareholder owning more than 5 percent of company issued capital.

TABLE 3
THE LARGEST AND THE SECOND LARGEST SHAREHOLDING OF 245 MALAYSIAN COMPANIES, 2002-2006

		Percentage Holding					
		LARGEST			SECOND		
	N	Mean	Median	Standard Deviation	Mean	Median	Standard Deviation
Average 2002-2006	1225	40.21%	40.41%	0.163	10.79%	9.18%	0.071
2002	245	40.50%	41.25%	0.161	11.23%	9.67%	0.075
2003	245	39.71%	39.87%	0.161	11.25%	10.42%	0.073
2004	245	40.13%	40.39%	0.165	10.49%	8.82%	0.069
2005	245	40.46%	40.54%	0.165	10.50%	8.73%	0.071
2006	245	40.26%	40.56%	0.164	10.46%	9.05%	0.068

Panel A of Table 4 highlights the largest shareholder ownership based on type of ownership. The results show that 73.71 percent of the sample companies are owned by a family group. The institutional-owned companies and foreign-owned companies are relatively smaller in the sample, where 4.90 percent and 7.51 percent are owned by an institutional shareholder and a foreigner, respectively. On average the holding of the largest shareholder which is categorized as a FAMILY is 37.68 percent. Even though FAMILY has a large presence as a large shareholder in the sample companies, the mean value of the shareholding is lower than the mean value of the holding of the largest shareholder that is categorized as GOVERMENT, INSTITUTIONAL and FOREIGN. Panel B shows that the number of companies with

significant second largest shareholding is high; where more than 75 percent of the observations have a second largest shareholder that owns more than 5 percent of equity holding.

TABLE 4
THE LARGEST SHAREHOLDER OWNERSHIP BASED ON THE TYPES AND CONCENTRATION FOR 245 MALAYSIAN COMPANIES, 2002-2006

PANEL A	N	Percentage Holding		
		Mean	Median	Standard Deviation
Type of largest shareholder				
FAMILY	903	37.68%	37.62%	0.158
GOVERNMENT	170	46.82%	45.88%	0.154
INSTITUTIONAL	60	49.33%	52.89%	0.177
FOREIGN	92	46.89%	40.41%	0.148
PANEL B	Frequencies			
The presence of other large shareholder				
SECOND5%	929			

The average amounts spent by companies on dividends, share buy-backs and total payouts are presented in Table 5. The average amount of dividends paid by the companies is RM38 million (median=RM7 million). The average amount of share buy-backs is RM15 million (median=RM1 million). Indeed, share buy-backs are not only less popular than dividends as a form of payout, but the amounts are much lower than the amount distributed by dividend-paying companies. The amounts distribute by companies to their shareholders using dividends and share buy-backs are shown in the last column of Table 5, with the average and median value of RM40 million and RM7 million, respectively.

TABLE 5
AMOUNT SPENT ON DIVIDENDS, SHARE BUY-BACKS AND TOTAL PAYOUTS BY DIVIDEND-PAYING COMPANIES, REPURCHASING COMPANIES AND DISTRIBUTING COMPANIES, RESPECTIVELY

Year	Average amount spent on dividends by dividend-paying companies (RM 000)		Average amount spent on share buy-backs by repurchasing companies (RM 000)		Average amount spent on total payouts by distributing companies (RM 000)	
	Mean	Median	Mean	Median	Mean	Median
2002	29,062.69	5,962.00	8,729.22	1,719.00	29,748.52	5,981.00
2003	31,944.50	5,867.00	3,630.93	600.00	31,837.48	5,836.00
2004	39,410.72	7,965.00	13,433.72	1,272.00	40,871.07	7,965.65
2005	39,637.92	8,439.00	27,709.58	1,566.85	45,072.54	8,249.50
2006	52,410.53	10,406.50	12,270.30	1,654.00	54,075.36	10,341.00
Average 2002-2006	38,520.09	7,600.00	15,600.21	1,352.00	40,447.73	7,530.00

Regression Analysis

Table 6 presents the results for the large shareholders' influence on the level of the total payout to earnings ratio. Consistent with prior studies, the analysis finds that the debt ratio is negatively and significantly associated with the total payout ratio (i.e. models 1 to 5). There is also evidence that the profitability level and company size are positively related with the total payout to earnings ratio, with

these relationships being significant at the 1 percent level and 10 percent level, respectively. The analysis also finds that the coefficient of the RISK variable is negative and statistically significant at the 1 percent level of confidence. However, companies' investment opportunities have no statistically significant impact on the level of total payout ratios.

In the model specification 1 in Table 6, the analysis finds that the coefficient for the variable representing the largest shareholding is positive and statistically significant at the 1 percent level. This suggests that the greater the holding of the largest shareholder in Malaysian companies, the higher the total payout ratio. Therefore, Hypothesis 1 of this study is being rejected. One explanation with respect to the positive and significant association between the largest shareholding and the total payout is that, instead of expropriation of minority shareholders, the monitoring function of dividends are more vital in these companies. Companies in which the largest shareholding is higher are subject to relatively higher entrenchment costs, therefore, the payment of higher dividends can act as a disciplining tool in such circumstances (Truong and Heaney 2007). Truong and Heaney (2007) also explain that the positive association may be consistent with the payment of higher payouts as compensation to the largest shareholder for providing monitoring services/benefits. This explanation is consistent with the Shleifer and Vishny (1986) view that companies pay higher dividends to attract large shareholders who are effective monitors. Another interpretation is based on the argument of Renneboog and Szilagyi (2006), where, instead of substitution effects, payouts and shareholder control act as complementary tools to alleviate agency conflicts. The model specification 1 also presents that the second largest shareholding variable, SECOND, has a positive sign, but the coefficient is not statistically significant.

In model specification 2, the analysis extends the model by including the variable SQLARGEST to test for the existence of a non-linear relationship between the magnitude of ownership of the largest shareholder and the total payout to earnings ratio. We find that the coefficient of the LARGEST and SQLARGEST variables are insignificant, thus, providing no evidence that different levels of ownership by the largest shareholder have a varying impact on the magnitude of the dividend payout ratio. This result is not consistent with research by Crutchley et al. (1999), Correia da Silva et al. (2004), Khan (2006) and Truong and Heaney (2007), who find a non-linear association between large shareholder ownership and dividend policy. In addition, this analysis incorporates the interaction between the large shareholder variables in model specification 3, to analyse further the relationship of large shareholders and the total payout ratio. The results confirm that the second largest shareholding has no influence on the magnitude of total payout of Malaysian companies.

In model specification 4 and 5, the analysis replaces the continuous variable, SECOND with the dummy variable, SECOND5%. The results show that the existence of a substantial second largest shareholder that owns at least 5 percent of the paid-up capital in a company, has a positive influence on the magnitude of total payout ratio. The coefficients for SECOND5% variable in both models are statistically significant at the 1 percent level, therefore, supporting Hypothesis 3. The coefficient of the LARGEST variable is also positive and statistically significant at the 1 percent significant level. This indicates that the presence of other large shareholders encourages companies to pay out higher dividends. This finding supports the argument about the positive monitoring role of other large shareholders, as proposed by Faccio et al. (2001) and Gugler and Yurtoglu (2003). This result also supports the La Porta et al. (2000) and Faccio et al. (2001) view that strong minority shareholders demand higher dividend payout as they anticipate that the controlling shareholder would expropriate them.

In analysing further the relationship between the large shareholders and the total payout ratio in model specification 5, the study finds that the coefficient for the interaction between the LARGEST and SECOND5% variables is negative and statistically significant at the 5 percent level. This indicates that companies with a higher largest shareholding and a substantial second largest shareholder, have a lower magnitude of the total payout ratio. A possible explanation may be that the largest shareholder collaborates with the substantial second largest shareholder in expropriating the corporate resources for their own private benefit. This reduces the pro-rata dividend payout to all shareholders. The results also support the conclusion by Faccio et al. (2001) on expropriation activities by the controlling shareholder in Asian companies, where lower dividend ratios are observed in these companies. The interaction term also

says that the greater is the largest shareholding in the presence of a second substantial shareholder, the less is the incentive for the second largest shareholder to demand dividend payout. This might suggest that a greater largest shareholding might have a bonding effect.

TABLE 6
THE INFLUENCE OF LARGE SHAREHOLDERS ON THE TOTAL PAYOUT TO EARNINGS RATIO

This table presents Tobit regressions to test the influence of the large shareholders on total payouts to earnings ratio The sample consists of 245 listed companies on the Bursa Malaysia between 2002 and 2006. TPE is total payouts divided by earnings after taxes and interest but before extraordinary items. DEBT is total debt over total assets. INV is the ratio of market capitalization to total assets. ROA is the ratio of earnings before interest and taxes to total assets. SIZE is the natural log of total assets. RISK is the standard deviation of the monthly share return. LARGEST is the proportional holding of the largest shareholder. SECOND is the proportional holding of the second largest shareholder. SECOND5% is a dummy variable equal to 1 if the second largest shareholder owns equal or more than 5 percent of the paid-up capital. z statistics are italicised. *, ** and *** denote 10%, 5% and 1% statistical significance level, respectively.

Independent Variables	1		2		3		4		5	
INTERCEPT	-2.102		-1.568		-2.134		-2.421		-3.043	
	-2.21	**	*-1.56*		***-2.13***	**	***-2.55***	**	***-2.92***	***
DEBT	-0.948		-0.950		-0.958		-1.091		-1.106	
	-2.19	**	***-2.20***	**	***-2.21***	**	***-2.52***	**	***-2.54***	**
INV	-.0486		-0.043		-0.050		-0.058		-0.058	
	-0.47		*-0.42*		*-0.42*		*-0.56*		*-0.56*	
ROA	1.950		2.041		1.974		1.882		1.873	
	2.72	***	***2.83***	***	***2.75***	***	***2.64***	***	***2.64***	***
SIZE	0.127		0.125		0.128		0.115		0.121	
	1.85	*	***1.81***	*	***1.85***	*	***1.66***	*	***1.73***	*
RISK	-3.317		-3.352		-3.257		-3.155		-3.040	
	-3.07	***	***-3.11***	***	***-3.02***	***	***-2.95***	***	***-2.84***	***
LARGEST	1.421		-1.603		1.411		1.789		2.845	
	2.95	***	-0.79		***1.72***	*	***3.65***	***	***3.17***	***
SECOND	1.247		1.610		3.122					
	1.30		*1.63*		*1.04*					
SQLARGEST			3.681							
			1.54							
LARGEST*SECOND					-4.302					
					-0.62					

Table 6 continued:

LARGEST*BUMIPUTERA					1.024				0.907	
					1.21				*1.09*	
SECOND5%							0.624		1.502	
							4.08	***	***3.33***	***
LARGEST*SECOND5%									-1.914	
									-2.08	**

Year dummies	Yes		Yes		Yes		Yes		Yes	
Industry dummies	Yes		Yes		Yes		Yes		Yes	
No. of observations	1225		1225		1225		1225		1225	
Left-censored observations	374		374		374		374		374	
Wald test	64.00	***	66.21	***	76.51	***	78.05	***	81.95	***
Log-likelihood	-1743.162		-1741.974		-1736.834		-1735.613		-1732.892	
Sigma u	1.057		1.059		1.059		1.065		1.088	
Sigma e	1.326		1.324		1.320		1.315		1.307	
Rho	0.389		0.390		0.387		0.396		.0409	

Table 7 shows the results on the determinant of total payout with particular emphasis on types of the largest shareholder. In model 6 and 7, the study re-estimates the basic model by including the FAMILY, GOVERNMENT and INSTITUTIONAL variables in the model. The dummy variable of a foreign shareholder (FOREIGN) is excluded from the analysis to avoid the circularity problem. The study does not find any evidences that the identity of the largest shareholder have any influence on TPE. The coefficients of the dummy variables of interest, are negative, but not statistically significant. The analysis further tests the notion that the types of controlling shareholder have influences on the magnitude of total payout by replacing the dummy variables that represent the types of the largest shareholder with the interaction between the LARGEST variable and FAMILY, GOVERNMENT and INSTITUTIONAL, respectively. The results in model 8 to 9 demonstrate that the interaction variables are not statistically significant.

The evidence does not provide support for the argument that the payout ratio is linked to the types of the controlling shareholder, particularly as suggested by Gugler (2003), Correia da Silva et al. (2004) Truong and Heaney (2007). A possible reason for the inconsistent results between our study and previous research is the difference in the institutional background of the countries and sample of the studies. Gugler (2003) use Austrian companies in his analysis, however, more than 80 percent of the sample are non-listed companies, with an average largest shareholding of 78.5 percent. Our study, on the other hand, focus on Malaysian listed companies with an average largest shareholding of 40.21 percent. Additionally, the influence of German banks are substantial on German companies, even though only 5.9 percent of companies are controlled (i.e. with largest shareholding more than 25 percent) by banks (Correia da Silva et al., 2004).

TABLE 7
THE INFLUENCE OF TYPES OF THE LARGEST SHAREHOLDER ON THE TOTAL PAYOUT TO EARNINGS RATIO

This table presents Tobit regressions to test the influence of types of the largest shareholder on total payouts to earnings ratio The sample consists of 245 listed companies on the Bursa Malaysia between 2002 and 2006. TPE is total payouts divided by earnings after taxes and interest but before extraordinary items. DEBT is total debt over total assets. INV is the ratio of market capitalization to total assets. ROA is the ratio of earnings before interest and taxes to total assets. SIZE is the natural log of total assets. RISK is the standard deviation of the monthly share return. LARGEST is the proportional holding of the largest shareholder. SECOND is the proportional holding of the second largest shareholder. SECOND5% is a dummy variable equal to 1 if the second largest shareholder owns equal or more than 5 percent of the paid-up capital. FAMILY is a dummy variable equal to 1 if the largest shareholder is a family group, 0 otherwise. GOVERNMENT is a dummy variable equal to 1 if the largest shareholder is the Government, 0 otherwise. INSTITUTIONAL is a dummy variable equal to 1 if the largest shareholder is an institutional shareholder, 0 otherwise. z statistics are italicised. *, ** and *** denote 10%, 5% and 1% statistical significance level, respectively.

Independent Variables	6		7		8		9	
INTERCEPT	-1.721		-2.123		-1.918		-2.273	
	-1.71	*	***-2.09***	**	***-2.01***	**	***-2.37***	**
DEBT	-0.919		-1.063		-0.911		-1.058	
	-2.12	**	***-2.45***	**	***-2.10***	**	***-2.44***	**
INV	-0.048		-0.057		-0.045		-0.055	
	-0.46		*-0.54*		*-0.44*		*-0.53*	
ROA	1.937		1.876		1.956		1.893	
	2.71	***	***2.64***	***	***2.74***	***	***2.66***	***
SIZE	0.114		0.106		0.114		0.106	
	1.64		*1.53*		***1.64***	*	*1.53*	
RISK	-3.295		-3.143		-3.309		-0.154	
	-3.05	***	***-2.93***	***	***-3.07***	***	***-2.95***	***
LARGEST	1.240		1.631		1.531		1.861	
	2.50	**	***3.22***	***	***1.89***	*	***2.28***	**
SECOND	1.349				1.356			
	1.40				*1.41*			
FAMILY	-0.202		-0.150					
	-0.67		*-0.50*					
GOVERNMENT	-0.166		-0.154					
	-0.47		*-0.43*					
INSTITUTIONAL	-0.331		-0.358					
	-0.75		*-0.81*					
FAMILY*LARGEST					-0.295		-0.208	
					-0.43		*-0.31*	
GOVERNMENT*LARGEST					-0.460		-0.459	
					-0.55		*-0.55*	
INSTITUTIONAL*LARGEST					-0.688		-0.788	
					-0.65		*-0.75*	
SECOND5%			0.608				0.612	
			3.94	***			***3.97***	***
Table 7 continued:								
Wald test	67.59	***	80.18	***	67.44	***	80.3	***
Log-likelihood	-1741.376		-1734.500		-1741.448		-1734.457	
Sigma u	1.054		1.063		1.053		1.062	
Sigma e	1.326		1.314		1.326		1.314	
Rho	0.387		0.396		0.387		0.392	

CONCLUSION

Based on agency perspectives, this paper examines the relationship between large shareholders and payout policy of Malaysian listed companies. The paper finds that large shareholders do influence the payout policy of Malaysian listed companies. It is observes that the higher the largest shareholding, the higher the total payout of the company. This does not support the classical agency view that large shareholder ownership and payouts substitute for each other to reduce agency conflicts. The results also reject the notion that large shareholders in Malaysia expropriate corporate resources for their own private benefit by reducing the level of payout ratio. The presence of the substantial second largest shareholder, who owns a minimum of 5 percent of the total paid-up capital, also has a positive and statistically significant influence on the total payout ratio. This indicates that the presence of other large shareholders

encourages the companies to distribute higher payouts. This finding supports the argument about the positive monitoring role of other large shareholders, as proposed by Faccio et al. (2001) and Gugler and Yurtoglu (2003). However, the study does not find significant evidence on the influence of the largest shareholder's identity on companies' payout level.

Overall, the paper finds that large shareholders in Malaysia have effects on the magnitude of total payout distribution. Future research can tests whether the concentration level of the largest shareholder have an impact on payout policy. Besides that, instead of focusing on the decision on how much to pay dividend/distribute funds, it is suggested that future research also focus on the decision of whether to distribute or not the funds of the corporation.

This study will add to the literature and enhance the understanding of the subject by providing evidence from an Asian country. In addition, the ongoing CG reform in Malaysia may result in payout policy being used as a CG tool, especially in an environment where conventional governance instruments have proven unsuccessful with regard to their monitoring function (Tam & Tan, 2007). Thus, this study may also provide insights and additional guidance for policy makers in improving the design of CG features.

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