Corporate Governance, Dividend Policy and Performance: Special Reference Listed Banking Institution in Sri Lanka

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Abstract— **This study explores the relationship between corporate governance, dividend policy and performance of listed banking institution in Colombo Stock Exchange (CSE). Corporate governance measured through Board independence, Board size, Board Meeting and CEO duality, Dividend policy was measured by Dividend yield and the Performance was measured by Return on Assets and growth. The Sample of this study composed of six (06) listed banking institutes in the CSE and the period of five (05) years from 2008 to 2012. The required data and information for the study were gathered from published annual reports, fact book, journals and website of listed banking institutions in CSE from 2008 to 2012. Descriptive and inferential statistics were used for this purpose. These studies find that dividend yield as the dividend policy indicator is significant and positively correlated to growth and CEO duality and negative to board independence. Return on assets (ROA) as performance indicator is positively correlated to board size and is significant. Outcomes of the study would be beneficial to the practitioners, investors, academicians, policy makers and others.**

Index Terms— **Corporate Governance, Dividend yield, Performance.**

I. INTRODUCTION

Corporate governance, the system by which companies are directed and controlled (Cadbury 1992), has succeeded in attracting a good deal of public interest over the years because of its apparent importance for the economic health of companies and society in general in both developed and developing countries. Corporate governance is defined as a process and structure used to direct and manage the business and affairs of a company towards enhancing business prosperity and corporate accountability. The ultimate objective is to realize long term shareholder value and also taking into account the interest of other stakeholders.

Corporate governance involves a set of relationship between a company's management, its board, its shareholders and other stakeholders. It provides the structure through which the objectives of the company are set, means of attaining those objectives and monitoring performance. It should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and facilitate effective monitoring. The presence of an effective corporate governance system helps to provide a degree of confidence that is necessary for the proper functioning of a market Economy (OECD principles 2004).

Dividend policy has an important role in financial decision making. Parallel with other decisions, Management should consider dividend policy decisions because if a firm decides to pay more dividends, it retains fewer funds for investment purposes, and the company may be forced to revert to capital markets to gain funds (Baker and Powell, 1992). Many studies such as Linter 1956;
Miller & Modigliani 1961; Feldstein & Green 1983; Baker and Powell 1992, 2000, regarding the dividend policy has been done and provided empirical evidence regarding the determinants of dividend policy. Yet, there is no indisputable explanation on what factors influence the dividend policy. The question of why firms pay dividends from their earnings still remains unexplained. This is known as the dividend puzzle in finance literature. (Alam Khan, 2009).

In the real world to determine the appropriate payout policy it is often a difficult task of balancing many conflicting forces. Pruitt and Gitman 1991 mention that the dividend payout has influence on shareholder wealth and firm's ability to participate in potential growth opportunities as investment, financing and dividend policy decisions are interrelated (Pruitt and Gitman, 1991).

Corporate performance is an important concept that relates to the way and manner in which financial resources available to an organization are judiciously used to achieve the overall corporate objective of an organization, it keeps the organization in business and creates a greater prospect for future opportunities. This study is a contribution to the ongoing debate on the examination of the relationship that exists between corporate governance mechanisms and firm performance. Mixed and tenuous findings have been made from previous studies especially those ones that were conducted in the developed nations, particularly USA, UK, Japan, Germany and France.

II. RESEARCH OBJECTIVE

Main objective of the study is to identify the impact of corporate governance, dividend policy on performance of listed Banking institution in Sri Lanka. To achieve above objective the following sub objectives were formulated
- To determine the impact of performance on dividend policy of banks listed on CSE.
- To determine the relationship between corporate governance and dividend policy for firms listed on CSE.

- To determine the impact of corporate governance practices on performance of banks listed on CSE.

III. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Corporate Governance and Performance

Velnampy T.(2013) in his research on corporate Governance and firm performance based on Sri Lankan manufacturing companies the results of the correlation showed that the determinants of corporate governance were not significantly correlated with ROE and ROA as the measures of firm performance. It meant companies do not properly practice corporate governance. The coefficient for all four variables board size, board committee, board structure, and board meeting were not significant. Further t values for all four variables of corporate governance are insignificant at 5% level. It means that these variables are not contributing to the performance measures of ROA and ROE.

Rajendran K. (2012) researched on Corporate Governance Practices and Its Impact on firm Performance with special reference to listed banking institutions in Sri Lanka. The results showed that overall, the correlations were low. But there are a number of statistically significant relationships. There was a significant relationship between corporate governance dimensions as composition of board, board committee, board size, board meeting, and firm performance.

Sanjai Bhagat & Brian Bolton (2009) researcher on Corporate Governance and Firm Performance: Recent Evidence. The results showed that corporate governance studies should consider director stock ownership as the most reliable measure of governance. There was investigating the relationship between SOX, governance and performance by examining how CEOs are disciplined following poor performance. There was that board independence and director stock ownership appear to be effective governance mechanisms for replacing the CEO following poor performance.

Ahmadu S, Aminu S. &Tukur G.(2005) in there research corporate governance mechanisms and firm financial performance in Nigeria The results showed that the coefficient estimate directors shareholding was significant (at 10%), although exhibiting a linear relationship; CEO duality had a negative and significant coefficient estimate, outside directors showed a significant and positive relationship with performance. Interestingly, debt turns out to be significant and positively associated with performance.

Sung Wook Joh (2001) researched on Corporate Governance and Firm Profitability: Evidence from Korea before the economic crisis. The results showed that Korea's weak corporate governance system offered few obstacles against controlling shareholder's expropriation of minority shareholders. Firm performance had been deteriorating over time even before the crisis occurred. Weak corporate governance systems allowed poorly managed firms to stay in the market and resulted in inefficiency of resource allocation despite low firm profitability for many years. Chronic low firm profitability over time is an important issue since it implies that nonperforming loans will increase and weaken the financial sector. Consequently, it would be helpful to examine the overall profitability of the corporate sector in evaluating the soundness of the financial sector and predicting crises. Yet, we still need more studies to examine whether and how poor firm profitability would have increased the possibility of crisis. If further studies support these results, policies that improve a country's corporate governance system can support its aggregate economic growth and stability.

Dividend and Performance

Samuel K.& Edward M.(2011) researched on dividend policy and bank performance in Ghana the results showed that dividend payout had a positive relationship with firm performance and this was significant at 2%. Banks that pay dividend increase their profitability. This means that as management pay out dividend, they tend to send out good signals about the bank's performance and therefore attracting more customers to deal with. When available resources of banks are reduced by the payment of dividend, it can also reduce agency cost between managers and owners thereby increasing their performance. Risk increases the performance of banks in Ghana. Although the size of a bank was found to be positively related to bank performance, the results were not significant. Growth in bank assets did not only influence bank performance positively but also significantly. It appears strongly that as banks grow their asset base, they are able to use the resources to generate more economic benefits.

Uwuigbe U., Jafaru J., & Ajayi A.,(2012) examined dividend policy and firm performance: a study of listed firms in Nigeria. The results find that there is a significant positive association between the performance of firms and the dividend payout of the sampled firms in Nigeria. The study also revealed that ownership structure and firm's size has a significant impact of the dividend payout of firms too.

Mobeen Ur Rehman., Aabid Hussain(2013) studied impact of dividend policy on performance of firms having stocks listed in an emerging stock market. They noted that the key indicators that do impact the performance of the firm and are also incorporated in the dividend policy of the firm. The impact can either be positive or negative depending upon the nature of variable. They taken sample of 475 companies and the data is the secondary one. Ratios have been computed of all the companies that basically determine the dividend policy and then the correlation tests have been run to see the whether the results are significant or not. They mentioned the variables that play a key role in determining the performance of the firms.

Corporate Governance and Dividend Policy

Dividend policy has become a major decision in corporate finance in recent times. Dividend is a distribution or appropriation of profit to shareholders. The amount is decided by the board of directors and is usually paid quarterly semi yearly or yearly depending on the policy of the firm. Study on dividend policy was provoked by Miller and Modigliani's (1961) research which concluded that under perfect capital markets dividends are not relevant. However, later investigations which lighten up the assumption of perfect market and documented the presence of market imperfections, such as information asymmetry, tax

consideration and agency cost discovered that dividend policy was indeed relevant to the value of a firm. Within corporate finance, dividend policy represents one of the most intensively researched topics that academics have studied. Numerous researchers have attempted to solve the "dividend puzzle" identified in Black (1976) but these studies have not yet arrived at an A common solution.

Ravichandran.S.,Susela Devi.S.,(2011) researched on Corporate Governance and Dividend Policy in Malaysia. They suggested that investigates the relationship between Investment Opportunity Set and dividend policy and if board size and board composition moderate this relationship in an emerging economy context. The free cash flow theory is empirically examined using a series of firm characteristics including size, return on assets, duality and debt to assets. The results support the theory that high growth firms make lesser dividend payouts. Further, in the interaction between high growth firms and board size and board composition, there is evidence to show that the negative relationship between Investment Opportunity Set and dividend payout is weaker for firms with a larger board size and with a corresponding larger number of independent directors representing the board.

Maniagi G.M., DencoMutirithia,J., Ondiek B.A., Okaka D.,& Musiega D.,(2013) researched on Corporate governance policy and performance. Special reference to banks listed on Nairobi Security Exchange Kenya. The results that dividend yield for bank listed on NSE as proxy of dividend policy is significant and positively correlated to business risk and growth opportunities GO thus tend to follow signaling hypothesis, also positively correlated to CEO duality but negative and significant to board independence as corporate governance proxies. ROA as a performance indicator is positively correlated to board size (number of directors) and is significant.

IV. CONCEPTUAL FRAME WORK

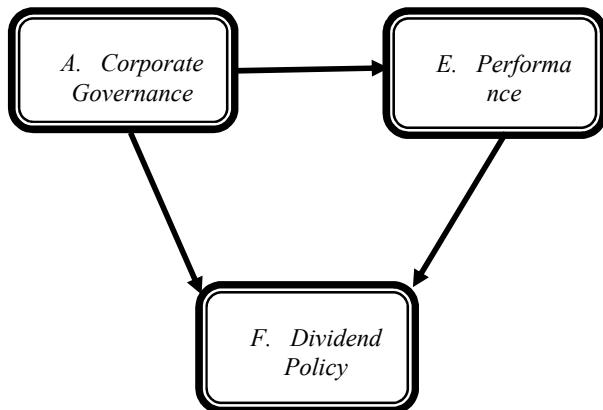The below frame work used in this research

Figure : 01 Frame Work

V. METHODOLOGY SCOPE

The scope of the study is listed banking institutions on CSE, Sri Lanka. Twelve banking are listed under banking sector.

Hence, out of twelve, only six banking institutions are selected for the study purpose as convenience. The banks include (1) Sampath Bank, (2) Commercial bank (3) Nation Trust Bank, (4) Seylan Bank, (5) National Development Bank,(6) Hatton National Bank.

VI. DATA SOURCES

In order to meet the objectives of the study, data were collected from secondary sources mainly from annual report of the selected banking instructions, which were published by CSE in Sri Lanka

VII. RELIABILITY AND VALIDITY

Secondary data for the study were drawn from audited accounts (i.e., Comprehensive income statement and financial position) of the concerned companies as fairly accurate and reliable. Therefore, these data may be considered reliable for the study. Necessary checking and cross checking were done while scanning information and data from the secondary sources. All these efforts were made in order to generate validity data for the present study. Hence, researcher satisfied content validity.

VIII. MODE OF ANALYSIS

After collecting data the researcher were analyses this data verify of techniques. In this study correlation and regression techniques are used for analysis.

OPERATIONALIZATION
Corporate Governance Measures

Variables	Measure
Board Independence	Ratio of number of non executive directors to the total number of directors
Board Size	Number of directors
CEO Duality	Dummy variable taking a value of 0 for firms with CEO as chairman otherwise 1
Board Meeting	Number of board meeting per year

Dividend Policy Proxy

Variable	Measure
Dividend Yield	Dividend per share / Market price per share

Performance Measure

Variable	Measure
Return on Assets	Earnings before interest and tax / Total Assets
Growth	Market price per shares /Book price per share

RESEARCH MODEL

Simple linear correlation model is formed to find out the relationship between corporate governance, dividend policy and performance: special reference listed banking institution in Sri Lanka. The correlation model will be formulated in the following manner:

$$Y = \beta_0 + \beta X + \ldots\ldots + E$$

Where Y is the dependent variable, β_0 is an intercept and β is the co-efficient of the independent variable. By substituting

both dependent and independent variables in the above model, the following models can be formed:

Model Specification

Dividend Policy and Performance

$DY = \beta_0 + \beta_1 GO + \beta_2 ROA + E$ | **Model 1**

Corporate Governance and Dividends Policy

$DY = \beta_0 + \beta_1 BI + \beta_2 BS + \beta_3 CEO + \beta_4 MT + E$ | **Model 2**

Corporate Governance and Performance | **Model 3**

$ROA = \beta_0 + \beta_1 BI + \beta_2 BS + \beta_3 CEO + \beta_4 MT + E$

Where:

DY: Dividend Yield

GO: Growth

BI : Board Independence

BS : Board Size

MT: Board Meeting

ROA: Return on assets

CEO: CEO Duality

$\beta_0 = \beta_1 = \beta_2 = \beta_3 = \beta_4$: Regression Parameters

IX. DATA ANALYSIS AND PRESENTATION

Descriptive analysis for the sample is performed on the dependent variable and the independent variables. The Analysis examines the mean, standard deviation skewness and kurtosis ranges of the data.

Table 01: Descriptive Statistics

Variables	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
					Statistic	Std. Error	Statistic	Std. Error
Dividend Yield	4.52	49.16	32.8900	15.78616	-1.375	.845	1.938	1.741
Return on Assets	.59	2.81	1.8117	.79406	-.408	.845	-.262	1.741
Growth	13.00	23.16	17.8650	4.24503	.132	.845	-1.910	1.741
Board Independence	.09	.78	.5100	.32735	-.914	.845	-1.870	1.741
Board Size	9.00	12.00	10.6667	1.03280	-.666	.845	.586	1.741
CEO Duality	.00	1.00	.8333	.40825	-2.449	.845	6.000	1.741
Board Meeting	12.80	19.00	15.0000	2.15407	1.556	.845	2.889	1.741

Table 01 illustrates that, descriptive statistics for all variables that the Average dividend yield of the Banking Institutions which registered in CSE is 32.89.The Minimum dividend yield is 4.52 and the maximum recorded as 49.16.Standard deviation of dividend yield is 15.78616. Board size has a minimum value of 9 directors on the board and a maximum of 12 directors and a mean of 10.66 directors. Board of independence shows that banks have a mean of 51% on non executive directors on board this is as per directive from central bank of Sri Lanka where they directs banks to not less than 50% of non executive directors.83.33% of banks on CSE have CEO also as the chairman of the board. Growth has a mean of 17.8650 while ROA has mean of 1.8117.

Results for Performance and Dividend Policy

Table 02: Correlation – Performance and Dividend Policy

		Return on Assets	Growth	Dividend Yield
Return on Assets	Pearson Correlation	1		
	Sig. (2-tailed)			
Growth	Pearson Correlation	.053	1	
	Sig. (2-tailed)	.921		
Dividend Yield	Pearson Correlation	.058	.844[*]	1
	Sig. (2-tailed)	.913	.034	

*. Correlation is significant at the 0.05 level (2-tailed).

It can be seen from the above table 02, dividend yield as proxy of dividend policy is positively correlated. Dividend yield is positively correlated with growth of bank Listed on CSE test statistic 0.844* p value < 0.05. When a bank pays higher dividend it relays information on the market of good future prospects. This leads to increase in stock prices as many outside investors would rush to purchase stock of the bank increasing their demand. This follows signaling hypothesis

and dividend relevant theory as the value of the firm increases when higher dividend is paid.

Dividend yield is positively correlated with return on assets ROA as a proxy for performance though not significant but negatively correlated to total debts to asset ratio and insignificant. This implies that the higher returns on assets signifies higher dividend yield. This could be due to

restrictive covenants given by lenders of loans and the central bank of Sri Lanka that limits increase in dividends making

dividends yield to move in opposite direction

Table 03: Coefficients of Performance and Dividend Policy

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	93.060	23.884		3.896	.030		
	Growth	-3.160	1.131	-.850	-2.795	.028	.897	1.103
	Return on Assets	-2.052	6.044	-.103	-.339	.757	.997	1.003

a. Dependent Variable: Dividend Yield

Table 04: Model Summary of Performance and Dividend Policy

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate	F	Sig F	Durbin Watson
1	.851[a]	.723	.539	10.71738	3.924	.045	.865

It is found that from the Table-03 and Table 04, we can observe model summary above multi collinearity problem can be tested using two variables, the variance inflation factor or tolerance test. Using tolerance test all the values are less than 1 showing that there is no multi collinearity problem and also when it's based on VIF the rule of the thumb agreed by many researchers is multi collinearity problem arises when VIF values are greater than 10. All the values are less than 10 then there is no multi collinearity problem (Besley1980) as sighted in (Jingyu Li 2003) Durbin Watson test the autocorrelation. If the value is less than 3 then there is no auto correlation problem. All values of Durbin Watson are less than 3.

The F value is 3.924*(p value < 0.05) is significant at 95% confidence level , showing the applicability of the overall model. The value of R square is .723 this implies that the independent variables in this model can explain 72.3% of variance in the dependent variable dividend yield DY while the remaining 27.7% can be attributed by other factors. The final equation will be DY =93.060 - 3.160GO -2.052ROA + ε.

Results for Corporate Governance and Dividend Policy
Table 05: Correlation for Corporate Governance and Dividend Policy

		Board Independence	Board Size	CEO Duality	Board Meeting	Dividend Yield
Board Independence	Pearson Correlation	1				
	Sig. (2-tailed)					
Board Size	Pearson Correlation	-.142	1			
	Sig. (2-tailed)	.788				
CEO Duality	Pearson Correlation	-.404	-.632	1		
	Sig. (2-tailed)	.427	.178			
Board Meeting	Pearson Correlation	.563	.342	-.910*	1	
	Sig. (2-tailed)	.244	.508	.012		
Dividend Yield	Pearson Correlation	-.419	-.660	.880*	-.718	1
	Sig. (2-tailed)	.409	.153	.021	.108	

*. Correlation is significant at the 0.05 level (2-tailed).

According to the table 05, Dividend yield is negatively correlated to board independence and insignificant. Thus as the proportion of non-executive directors decrease dividend yield will have to increase. Dividend yield is positively correlated to CEO duality test statistic 0.880* p value is < 0.05 which indicate that it is significant at 95% confidence level. Thus as the CEO takes up doubles up as the chairman of the bank then the dividend yield of the bank will increase this could be due to the consolidation of authority giving the chairman to push for higher dividend yield and allows a person to have greater understanding and knowledge of firm. Dividend yield is negatively correlated with board size and Board Meeting but its weak and not significant. Thus these two variables of corporate governance and dividend yield move in opposite direction.

Table 07: Coefficients of Corporate Governance and Dividend Policy

Model	Unstandardized Coefficients		Standardized Coefficients			Collinearity Statistics	
	B	Std. Error	Beta	t	Sig.	Tolerance	VIF
1 (Constant)	-60.264	293.872		-.205	.871		
Board Independence	-13.345	24.441	-.277	-.546	.682	.553	1.809
Board Size	-1.470	11.414	-.096	-.129	.918	.255	3.926
CEO Duality	50.820	62.169	1.314	.817	.564	.055	18.201
Board Meeting	4.886	9.860	.667	.495	.707	.078	12.747

a. Dependent Variable: Dividend Yield

Table 08: Model Summary of Corporate Governance and Dividend Policy

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	F	Sig F	Durbin-Watson
1	.926[a]	.858	.290	13.30230	1.510	.539	1.154

a. Predictors: (Constant), Board Meeting, Board Size, Board Independence, CEO Duality
b. Dependent Variable: Dividend Yield

The above table 07 and table 08, there is no multi collinearity problem as all the VIF values are less than 10 which is acceptable by many researchers. Also there is no auto correlation problem in the regression model used as the Durbin Watson rule of value 1.154 is less than 3. The F value is 1.510 is not significant, showing the applicability of the overall model. The value of R square is .858 this implies that the independent variables in this model can explain 85.8% of variance in the dependent variable dividend yield while the remaining 14.2% can be attributed by other factors. The regression equation will be

DY =-60.264 -13.345BI -1.470BS + .50.820CEO +4.886MT + **E**

Results for Corporate Governance and Performance
Table 09: Correlation of Corporate Governance and Performance

		Board Independence	Board Size	CEO Duality	Board Meeting	Return on Assets
Board Independence	Pearson Correlation	1				
	Sig. (2-tailed)					
Board Size	Pearson Correlation	-.142	1			
	Sig. (2-tailed)	.788				
CEO Duality	Pearson Correlation	-.404	-.632	1		
	Sig. (2-tailed)	.427	.178			
Board Meeting	Pearson Correlation	.563	.342	-.910[*]	1	
	Sig. (2-tailed)	.244	.508	.012		
Return on Assets	Pearson Correlation	-.234	.325[*]	-.375	.506	1
	Sig. (2-tailed)	.655	.029	.463	.305	

*Correlation is significant at the 0.05 level (2-tailed).

It can be seen from the above table 09, Return on assets as a proxy of performance is positively correlated with board size (0.325* p value <0.05) which is significant at 95% confidence level. This implies that for banks listed on CSE a large board with varied specializations tends to be keen with all activities of the bank which ensures higher returns on assets compared to when the board size is small.

Table 10: Coefficients of Corporate Governance and Performance

Model	Unstandardized Coefficients		Standardized Coefficients			Collinearity Statistics	
	B	Std. Error	Beta	t	Sig.	Tolerance	VIF

1	(Constant)	-22.787	6.656		-3.424	.045		
	Board Independence	-1.875	.554	-.773	-3.388	.043	.553	1.809
	Board Size	.568	.259	.739	2.196	.027	.255	3.926
	CEO Duality	4.587	1.408	2.358	3.258	.040	.055	18.201
	Board Meeting	1.045	.223	2.835	4.679	.134	.078	12.747

a. Dependent Variable: Return on Assets

Table 11: Model Summary of Corporate Governance and Performance

Model	R	R Square	Adjusted R ^{2}	Std. Error of the Estimate	F	Sig F	Durbin-Watson
1	.985[a]	.971	.856	.30128	8.433	.045	1.154

a. Predictors: (Constant), Board Meeting, Board Size, Board Independence, CEO Duality
b. Dependent Variable: Return on Assets

According to the table 10 and table 11, there is no multi collinearity problem as all the VIF values are less than 10 which is acceptable by many researchers. Also there is no auto correlation problem in the regression model used as the Durbin Watson rule of value is less than 3.The F value is 8.433*(p value < 0.05) is significant at 95% confidence level, showing the applicability of the overall model. The value of R square is .971 this implies that the independent variables in this model can explain 97.1% of variance in the dependent variable ROA while the remaining 2.9 % can be attributed by other factors. The regression equation will be
ROA =-22.787-1.875BI + 0.568BS +4.587CEO + 1.045MT + **E**

CONCLUSION

This study examined corporate governance, dividend policy and performance: special reference listed banking institution in Sri Lanka. Banking Listed on CSE have adopted signaling hypothesis where banks with high dividend yield tend to signal good future prospects leading to high growth of the firms. This explains the positive correlation of dividend yield and growth which is taken as market price to book ratio of stock. The finding suggests that dividend yield as the dividend policy indicator is significant and positively correlated to growth and CEO duality and negative to board independence. Return on assets (ROA) as performance indicator is positively correlated to board size and is significant.

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