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Effect of Free Cash Flow, Profitability, Institutional Ownership, Firm Size and Leverage on Dividend Payout Ratio

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Abstract: This study aims to empirically examine the effect of free cash flow, profitability, institutional ownership, firm size and leverage on the dividend payout ratio of companies listed on the Jakarta Islamic Index (JII) for 2018-2021. This type of quantitative research uses secondary data obtained from company financial statements obtained from the IDX or company websites, with data collection techniques using purposive sampling method and obtained 52 samples as research material. The dependent variable in this study is the dividend payout ratio, while the independent variables are free cash flow, profitability, institutional ownership, firm size and leverage. The analysis used is multiple linear regression. The results of this study indicate that free cash flow, profitability, institutional ownership has no effect on the dividend payout ratio. Meanwhile, firm size and leverage variables simultaneously influence the dividend payout ratio.

Keywords: free cash flow, profitability, institutional ownership, firm size, dividend payout ratio.

1. Introduction

The capital market is an alternative source of long-term funds among various other alternative sources of funds for companies. The capital market is also a means for companies to increase long-term funding needs by selling stocks or bonds (Hartono, 2003 in Kristianawati, 2013).

Investment activity is an activity that has various types of risks and uncertainties that are often difficult for investors to predict. To reduce the possibility of risk and uncertainty, investors can seek various types of information, both information about company performance and other relevant information such as the economic and political situation of a country. The information obtained from the company is usually based on the company's performance as reflected in the financial statements (Laksono, 2006 in Harun, 2018).

The goal of an investor in investing his money in a company is to obtain returns in the form of dividends (dividend yield) or income from the difference between the selling price and the purchase price of shares (capital gain/loss). On the other hand, the company wants to gain profits from the investment of the investors it manages to finance the company's operations. Companies must carefully decide whether to reinvest company profits as retained earnings to generate capital gains or distribute them to shareholders in the form of dividends. Companies must apply the right dividend policy for optimal results. (Aulia, 2011 in Aaron, 2018).

Company management limits dividend payments because it reduces company profits or because of profitable investment opportunities. This happens because the company's profits are used as a source of internal funding. Whereas on the other hand, investors expect dividend payments to be evenly distributed or tend to increase from year to year because stable dividend payments can increase investor confidence in the company. (Aulia, 2011 in Aaron, 2018).

Dividend payment itself is influenced by dividend politics related to the determination of the distribution of income (earnings) between the use of income to be paid to shareholders as dividends or used for the company which means it is retained in the company. (Riyanto, 2001 in Harun, 2018). Dividend policy can be an elemental aspect for investors to evaluate the company. This is because dividend policy can affect stock prices.

Jakarta Islamic Index (JII) is an Islamic stock index that was first launched on the Indonesian capital market on July 3, 2000. JII's constituents only consist of the 30 most liquid Islamic stocks listed on the IDX. Just like ISSI, the review of sharia stocks which are constituents of JII is carried out twice a year, in May and November, following the DES review schedule by the OJK. (Irman et al., 2020).

2. Literature Review and Hypothesis

Agency Theory

Agency theory is a relationship between the owners (principle) and managers (agents) who in this case are the managers of the company. Where the owner is a business entity that has delegated his authority to manage the company to the manager. This can be done by giving or delegating some authority related to decision making to agents (Jensen and Meckling, 1976) in (Kafata, 2018). In this case, the owner gives authority and authority to the manager to operate the company in his interests. The authorities and responsibilities of managers and owners are regulated in a work contract and are based on mutual agreement (Prasetio and

Suryono, 2016 in Kafata, 2018).

Agency theory explains that agency relationships arise when one or more people (principal) hire another person (agent) to provide a service and then delegate decision-making authority to the agent (Jensen and Meckling, 1976 in Awalina, 2018). Companies that separate control and ownership functions will face agency problems because the interests of the two are different. On the one hand, shareholders want managers to make the best decisions that benefit shareholders, but on the other hand managers also want profits for themselves. The existence of agency problems between agents and principals will cause agency costs. The more frequent the level of occurrence of conflicts, the more agency costs will be generated (Jensen and Meckling, 1976 in Awalina, 2018).

Signal Theory

According to Brigham and Houston (2006:40) in (Kafata, 2018)Signals or cues are the taking of an action by the company for investors to provide guidance on how management views the company's prospects. The following signals indicate what information is related to what management has done to realize the owner's expectations.

Meanwhile according to Ramadhan (2018) in (Firnanda, 2022)Signal theory is an action taken by company management to provide guidance to investors about how management assesses the company's prospects. Companies that experience bad news can show that this is a bad signal for investors to invest their capital. Conversely, companies that experience good news will be a good signal for investors. One of the company information issued by the company is financial statements.

Dividend Payout Ratio

According to (Mardiyati, 2014) The Dividend Payout Ratio is the ratio between the total dividends paid and the net profit earned and is usually presented in percentage form. This ratio will determine the amount of profit that will be distributed in the form of dividends to shareholders and profits that will be retained as a source of corporate funding. The Dividend Payout Ratio shows the percentage of profit earned by the company which is paid in the form of cash dividends to shareholders, so it can be concluded that if a company has a high dividend payout ratio, the amount of profit that will be paid as dividends to shareholders or investors is also high.

Free Cash Flow

According to (Brigham & Houston, 2011) in (Ramdhany et al., 2020)Free cash flow is "the cash flow that is actually available to be paid to investors (shareholders and debt owners) after the company has invested in fixed assets, new products, and working capital needed to maintain ongoing operations. ." More specifically, the operating value of a company will depend on its estimated future free cash flows, which are expressed as after-tax operating profit minus investment in working capital and fixed assets needed to sustain the business. So free cash flow reflects the cash that is actually available to be paid out to investors. Therefore, managers make their companies more valuable by increasing their free cash flow.

H1: Free Cash Flow has an affect on the Dividend Payout Ratio.

Profitability

According to Santoso (2009) in (Puspita, 2017)Profitability is a measure that shows the overall performance of the company or how efficient the management of assets, liabilities and equity is. Considering that the company's goal is to make a profit, the profitability ratio is one of the important financial ratios. This element directly affects cash flows in the future resulting from increasing profits and or an increase in the value of the company's shares. The measurement ratio used in this study to measure profitability is Return On Assets (ROA). (Brigham & Houston, 2011) in (Febriani & Sari, 2019)stated Return On Assets is the ratio of net income to total assets measuring the return on total assets after interest and taxes

H2 = There is an effect of the profitability ratio as measured using Return on Assets (ROA) on the amount of the Dividend Payout Ratio (DPR).

Institutional Ownership

Institutional ownership is the number of shareholdings by institutional investors outside the company. Institutional ownership is calculated by dividing the number of shares owned by the institution by the number of shares outstanding. According to Listyani (2003) in (Suhartono, 2015), institutional ownership is the portion of shares owned by institutions at the end of the year as measured in percentages. A high level of institutional share will result in more intensive monitoring efforts thereby limiting opportunistic behavior of managers, namely managers reporting profits opportunistically to maximize their personal interests.

H3: Institutional ownership has an effect on the Dividend Payout Ratio.

Firm Size

Company size describes the size of a company where large companies will find it easier to get loans from outside in the form of debt or share capital because usually large companies are accompanied by a fairly good reputation in the eyes of the public. According to (Sartono, 2016) in(Febriani & Sari, 2019)argues that, large companies will find it easier to obtain capital in the capital market compared to small companies. According to (Palupi, 2011) in(Febriani & Sari, 2019)states that, size reflects the size of the company. Larger companies will need more funds than small companies. (Brigham & Houston, 2011) in(Febriani & Sari, 2019)Company size is as follows: Company size is a measure of the size of a company which is indicated or assessed by total assets, total sales, total profits, tax expenses and others.

H4: *Firm Size* has an effect on the Dividend Payout Ratio.

Leverage

According to Santoso (2009) in(Puspita, 2017)This ratio is a measure that shows the company's ability to carry out its business stably, which is measured by considering the company's ability to pay interest on its debts and ultimately pay these debts on time. According to Santoso (2009) in(Puspita, 2017)One of the leverage ratios can be measured using the debt to equity ratio (Debt to Equity Ratio). This ratio compares the amount of interest-bearing loans drawn by the company with shareholder equity.

H5: Leverage as measured by DER has an effect on the Dividend Payout Ratio.

Research Model

To facilitate understanding of the effect of Free Cash Flow, profitability, ownership structure and Firm Size on the dividend payout ratio, it can be described as follows:

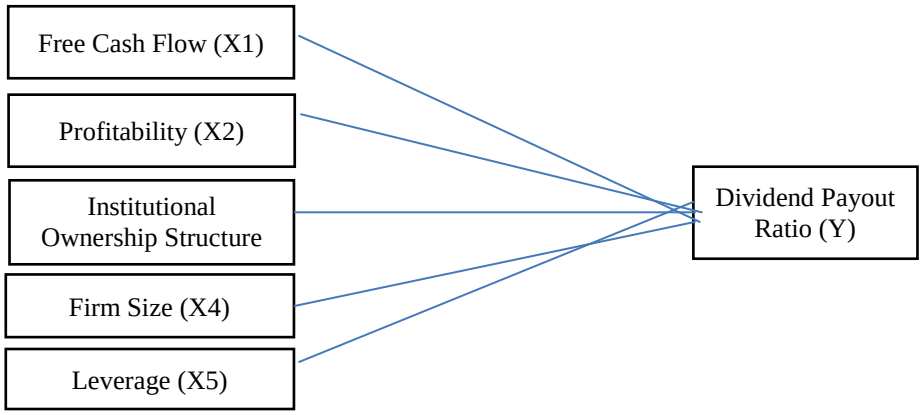

Figure 1
Research Model

3. Research methods

Population And Sample

The population used is all companies registered in the Jakarta Islamic Index (JII) for 2018-2021. The company also publishes an annual report and presents a corporate governance report in its annual financial report. Through sample selection, 19 companies were obtained that were consistently registered as members of JII from 2018-2021. This can be shown shown in table 4.1 below:

Table 4.1
Research Sampling Criteria

SAMPLE CRITERIA	
Companies registered in JII 201-2021.	30
1. Companies are not routinely listed in the Jakarta Islamic index (JII) in the 2018-2021 period.	(11)
2. The company does not routinely publish a complete annual report for the 2018-2021 period.	0
3. The company experienced losses during the 2018-2021 period.	0

4. The company does not routinely distribute dividends to investors during the 2018-2021 period.	(6)
Research Sample	13
Total Sample (n x Sample Period) (13 x 4 Years)	52

This study uses the measurement of each variable as follows:

Variable	Indicator
Dividend Payout Ratio	$Deviden\ Payout\ Ratio = \frac{Deviden\ Per\ Share}{Earning\ Per\ Share}$
Free Cash Flow	$FCF = \frac{Operating\ Cash\ Flow}{Total\ Assets}$
Profitability	$ROA = \frac{Total\ Net\ Income\ After\ Tax}{Total\ Assets}$
Institutional Ownership	$INST = \frac{The\ number\ of\ shares\ owned\ by\ the\ institution.}{Total\ outstanding\ shares}$
Firm Size	$Firm\ SIze = \ln(total\ aktiva)$
leverage	$DER = \frac{Total\ Debt}{Total\ Equity}$

Data analysis technique

In this study, testing the hypothesis using multiple regression analysis. Multiple linear regression method was used to determine the correlation of each independent variable to the dependent variable.

$$DPR = a + \beta 1FCF + \beta 2ROA + \beta 4KI + \beta 5SIZE + \beta 6LEV + e$$

Information
DPR = Dividend Payout Ratio
FCF =*Free Cash Flow*
ROA =*Return on Assets*
KI = Institutional Ownership
SIZE =*Firm Size*
Lev =*leverage*
a = Constant Regression Equation
β = Regression Coefficient
e = Determinant of Error

4. Results and Discussion

Descriptive Statistical Analysis

Descriptive statistical analysis is used to provide an overview or description of a data. In this study descriptive statistical analysis was seen using the minimum value, maximum value, average value and standard deviation.

Descriptive Statistical Analysis Test

	N	Minimum	Maximum	Means	std. Deviation
FCF	52	-,02	,42	,1550	,10116
ROA	52	,01	,47	,1096	,09053
KI	52	,44	,85	,6017	,11494
SIZE	52	30,53	33,26	31.5256	,82102
Lev	52	,19	3,41	,8306	,67251
DPR	52	,05	5,13	,7492	,77991
Valid N (listwise)	52				

After performing descriptive statistical analysis using SPSS 25, the data in the table above shows that column N is valid data and used in this study as many as 52 data samples according to the number of observations found in this study. Based on these results it can be concluded as follows:

The dependent variable, namely the Dividend Payout Ratio, is known to have a minimum DPR value of 0.05 and a maximum value of 5.13 with an average of 0.7492 at a standard deviation of 0.77991. The independent variable, Free Cash Flow, is known to have a minimum FCF value of -0.02 and a maximum value of 0.42 with an average of 0.1550 at a standard deviation of 0.10116. Profitability variable as measured using Return on Assets (ROA) produces a minimum value of 0.01 and a maximum value of 0.47 with an average of

0.1096 at a standard deviation of 0.09053. The Institutional Ownership variable shows a minimum value of 0.44 and a maximum value of 0.85 with an average of 0.6017 at a standard deviation of 0.11494. The Firm Size variable shows a minimum value of 30.53 and a maximum value of 33.26 with an average of 0.8306 at a standard deviation of 0.67251.

Classic assumption test

Normality test

The normality test was carried out using the monte carlo method, by looking at the significance value at 0.05. If the resulting significance value is > 0.05, the data is normally distributed.

Normality test
Monte Carlo Test

	Unstandardized Residuals
N	52
asymp. Sig (2-tailed)	0.002
Monte Carlo Sig. (2-tailed)	0.121

From the results of the Kolmogorov-Smirnov test with Monte Carlo above, the Monte Carlo Sig value is generated. (2-tailed) of 0.121. These results can be concluded that the residual data in this regression model is normally distributed because the value of Monte Carlo Sig. (2-tailed) above 0.05.

Multicollinearity Test

The multicollinearity test was carried out with the aim of testing the regression model and found a correlation between the independent variables. The multicollinearity test is carried out by looking at the tolerance value and the Variance Inflation Factor (VIF) value, if the tolerance value is > 0.10 and the VIF value is <10 then there are no symptoms of multicollinearity in the regression model.

Multicollinearity Test

Model	**Collinearity Statistics**		**Conclusion**
	tolerance	**VIF**	
(Constant)			
Cash Flow Fees	0.189	5,284	No multicollinearity
ROA	0.150	6,672	No Multicollinearity
Institutional Ownership	0.507	1,971	No Multicollinearity
Firm Size	0.685	1,459	No Multicollinearity
leverage	0.624	1,602	No Multicollinearity

From the results of the multicollinearity test analysis above, VIF values were obtained ranging from 1.390 to 2.244, all of which had values below 10. Thus the regression model of this study did not contain symptoms of multicollinearity. and can be used for further analysis.

Heteroscedasticity Test

Heteroscedasticity test aimsto test whether in the regression model there is an inequality of variance from one observation residual to another. In this research, the test uses Rank Spearman.

Spearman's Rank Test

Variable	*Sig.*	Information
FCF	0.432	There is no Heteroscedasticity
ROA	0.710	There is no Heteroscedasticity
KI	0.407	There is no Heteroscedasticity
SIZE	0.321	There is no Heteroscedasticity
Lev	0.063	There is no Heteroscedasticity

Based on the table, it shows that the significance value of FCF is 0.432, ROA is 0.710, KI is 0.407, SIZE is 0.321, LEV is 0.063. Based on this significance value, it can be concluded that the regression model does not have heteroscedasticity, so it can be used for further testing.

Autocorrelation Test

The autocorrelation test is a test carried out to test whether in the linear regression model there is a correlation between the confounding errors in period t and the confounding errors in t-1 (previously). If there is correlation, then it is called an autocorrelation problem (Ghonzali, 2016: 107). The autocorrelation test was carried out by looking at the DW (durbin Watson) numbers (du < d < 4 – du).

Autocorrelation Test

Model	Durbin Watson
1	**2.148**

From the table above it is known that Durbin Watson in this regression model is 2.148, the dU value is 1.7694 and (4-dU) = 2.2304. It can be said that the data does not have autocorrelation if dU < dcount < 4 – dU. So if entered into the equation is 1.7694 < 2.148 < 2.2304 . So as the basis for decision making in Durbin Watson above, it can be concluded that there are no autocorrelation symptoms.

Multiple Linear Regression Analysis

Multiple linear regression analysis is used to test the effect of the independent variables on the dependent variable, namely the company's financial performance.

Multiple Linear Regression Analysis

Model	nstandardized Coefficients		Standardized Coefficients	Q	Sig
	B	std. Error	Betas		
(Constant)	10,467	4,685		2,234	.030
FCF	2,124	2,213	,276	,960	,342
ROA	-1,824	2,779	-,212	-,657	,515
KI	-,749	1,190	-,110	-.630	,532
SIZE	-,312	,143	-,329	-2.178	.035
Lev	,536	, 183	,462	2,922	,005

From the results of the multiple linear regression above, the regression equation model developed in this study is as follows:

DPR = 10.467 + 2.124 FCF – 1.824 ROA – 0.749 KI – 0.312 SIZE + 0.536 LEV + e

a. The constant has a value of 10.467, stating that the dividend payout ratio is 10.467 with the assumption that FCF, ROA, KI, SIZE, LEV are 0.
b. The FCF regression coefficient has a value of 2.124. Show that the higher the FCF, the higher the dividend payout ratio. Conversely, the lower the FCF, the lower the dividend payout ratio.
c. The ROA regression coefficient has a value of -1.824. Show that the higher the ROA, the lower the dividend payout ratio. Conversely, if the lower the ROA, the dividend payout ratio will increase.
d. The regression coefficient for KI has a value of -0.749. Show that the higher it is proportion KI, then the dividend payout ratio will be lower. Conversely, if it is lower proportion KI, it will increase the dividend payout ratio.
e. The SIZE regression coefficient has a value of -0.312. Show that the higher the SIZE, the lower the dividend payout ratio. Conversely, the lower the SIZE, the higher the dividend payout ratio.
f. The LEV regression coefficient has a value of 0.536. Show that the higher the LEV, the higher the dividend payout ratio. Conversely, the lower the LEV, the lower the dividend payout ratio.

Simultaneous Test (Test F)

This test is carried out by comparing the significance value indicated by the significance of F with the level of significance taken. In this case using a significance level of 0.05. If the significant value <0.05, the independent variables jointly affect the dividend payout ratio variable.

Simultaneous Test (Test F)

ANOVAa						
Model		Sum of Squares	df	MeanSquare	F	Sig.
1	Regression	8,768	5	1,754	3,625	,008b

	residual	22,253	46	,484		
	Total	31,021	51			
a. Dependent Variable: DPR						
b. Predictors: (Constant), LEV, SIZE, FCF, KI, ROA						

The table above shows that the independent variables free cash flow, return on asser, institutional ownership, firm size and leverage on the dividend payout ratio have a significance value of 0.008, which is smaller than the 0.05 significance level. So it can be said that in this study the variables of free cash flow, return on asser, institutional ownership, firm size and leverage simultaneously (simultaneously) affect the dividend payout ratio.

Determination Test (R^2)

The coefficient of determination (R2) is used to measure how far the model's ability to explain the variation in the dependent variable.

Determination Coefficient Test (R^2)

R	R Square	Adjusted R Square
.532	.283	.205

The results of the analysis of the coefficient of determination, the resulting coefficient of determination (Adjusted R Square) of the research model is 0.205. From these results it can be concluded that the magnitude of the variation in the independent variable influencing the dividend payout ratio is 20.5% and the remaining 79.5% is influenced by other variables not included in the regression model.

Partial Test (t test)

The t test is used to see the significance of the effect of the independent variables partially on the dependent variable. In this case using a significance level of 0.05. If the significant value is <0.05 then the independent variable affects the dependent variable.

Partial Test (t test)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	std. Error	Betas		
1	(Constant)	10,467	4,685		2,234	.030
	FCF	2,124	2,213	,276	,960	,342
	ROA	-1,824	2,779	-,212	-,657	,515
	KI	-,749	1,190	-,110	-.630	,532
	SIZE	-,312	,143	-,329	-2.178	.035
	Lev	,536	, 183	,462	2,922	,005

Based on the table above, it is explained that the value of each variable is as follows:

a. The results of the t test in the table above show that the significance value of free cash flow is 0.342, which is greater than the significance level of 0.05 (0.342 > 0.05). It can be said that, in this study, free cash flow has no effect on the dividend payout ratio. Thus the first hypothesis (H3) is rejected.
b. The results of the t test in the table above show that the significance value of return on assets is 0.515, which is greater than the significance level of 0.05 (0.515 > 0.05). It can be said that in this study the return on assets has no effect on the dividend payout ratio. Thus the second hypothesis (H2) is rejected.
c. The results of the t test in the table above show that the significance value of institutional ownership is 0.532, which is greater than the significance level of 0.05 (0.532 > 0.05). It can be said that in this study institutional ownership has no effect on the dividend payout ratio. Thus the third hypothesis (H3) is rejected.
d. The results of the t test in the table above show that the significance value for firm size is 0.035, which is smaller than the significance level of 0.05 (0.035 <0.05). It can be said that in this study firm size has an effect on the dividend payout ratio. Thus the fourth hypothesis (H4) is accepted.
e. The results of the t test in the table above show that the significance value for leverage is 0.005, which is smaller than the significance level of 0.05 (0.005 <0.05). It can be said that in this study leverage affects the dividend payout ratio. Thus the fifth hypothesis (H5) is accepted.

Discussion

1. The Effect of Free Cash Flow on the Dividend Payout Ratio

Through the t test in the table shows that the Free Cash Flow has no effect on the Dividend Payout Ratio. So statistically it was found that the first hypothesis (H1) was rejected. This shows that the size of the free cash flow does not affect the high or low dividend distribution. The results of this study support the results of the research expressed by Kafata (2018) which states that the Free Cash Flow has no effect on the Dividend Payout Ratio.

Brigham and Houston (2006:58) reveal that free cash flow reflects the amount of cash generated by a business for its shareholders, in a given year. A company that generates high cash flow does not always report a high amount of cash on its balance sheet. Companies do not only need the availability of cash in order to distribute dividends. Companies must also have retained earnings and the board of directors must take formal action so that a company can distribute dividends to its shareholders.

2. The Effect of Profitability on the Dividend Payout Ratio

Through the t test in the table shows that Profitability as measured by ROA has no effect on the Dividend Payout Ratio. So statistically it was found that the second hypothesis (H2) was rejected. The results of this study are in line with research conducted by Febriani & Sari (2019) which states that Return on Assets has no effect on the Dividend Payout Ratio.

Return On Assets (ROA) describes a company's ability to earn profits from the capital it uses. ROA is measured by comparing net profit after tax with total assets. The amount of profitability obtained by the company does not guarantee that the dividends distributed will also increase. This is because the company retains profits to be used as additional capital, investment or to pay debts.

3. The Effect of Institutional Ownership on the Dividend Payout Ratio

Through the t test in the table shows that Institutional Ownership has no effect on the Dividend Payout Ratio. So it can be interpreted that the third hypothesis (H3) is rejected. The results of this study are in line with the research of Awalina (2018) which states that institutional ownership has no effect on the Dividend Payout Ratio.

Institutional ownership is the portion of shares owned by institutions at the end of the year as measured in percentages. Regardless of the proportion of shares owned, it will not affect the percentage of shares received by the institution. The number of shares to be received by the institution has been determined at the General Meeting of Shareholders (GMS).

4. Effect of Firm Size on the Dividend Payout Ratio

Through the t test in the table above, it shows that Firm Size has an effect on the Dividend Payout Ratio. So it can be interpreted that the fourth hypothesis (H4) is accepted. This research is in line with research conducted by Julita (2021) which states that partially there is an effect of Firm Size on the Dividend Payout Ratio.

Firm Size is the size of the company, size shows the theoretical basis for the effect of size on the very strong Dividend Payout Ratio. Large companies are not necessarily able to manage their assets properly. Large companies with large levels of assets require large funds to carry out their operational activities. So that it can reduce profits and reduce the amount of dividends to be distributed.

5. The Effect of Leverage on the Dividend Payout Ratio

Through the t test in table 4.11 above, it shows that leverage measured using the Debt to Ratio (DER) has an effect on the Dividend Payout Ratio. So it can be interpreted that the fifth hypothesis (H5) is accepted. This result is in line with research conducted by Puspita (2017) which states that leverage affects the Dividend Payout Ratio.

Santoso (2009) states that DER is a measure that shows a company's ability to carry out its business stably, which is measured by considering the company's ability to pay interest on its debts and ultimately pay these debts on time. Companies that can manage their debts to the maximum and aim for business development will increase profits so that the dividends distributed by the company will also increase.

5. Conclusion

Based on the results of the data analysis described in the previous chapter, the following conclusions can be drawn:

1. The Free Cash Flow (FCF) variable in companies registered on JII in 2018-2021 has no effect on the Dividend Payout Ratio.

2. The Profitability variable as measured using Return on Assets (ROA) for companies registered on JII in 2018-2021 has no effect on the Dividend Payout Ratio.
3. The institutional ownership (IC) variable in companies registered on JII in 2018-2021 has no effect on the Dividend Payout Ratio.
4. The Firm Size variable in companies registered on JII in 2018-2021 has an effect on the Dividend Payout Ratio.
5. Leverage variables in companies registered on JII in 2018-2021 have an effect on the Dividend Payout Ratio.

6. Suggestion

With the limitations in this study, the authors provide suggestions to further researchers as follows:

1. For future researchers, it is expected to increase the number of samples with other types of industries. So that it is expected to produce better research results.
2. Future studies are expected to add other variables not included in this study, both financial and non-financial information which are thought to have an influence on predicting the dividend payout ratio.
3. Further research is expected to increase the observation period so that it is expected to produce better research results.

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