

Corporate Governance and Cash Dividend Policy: Evidence from Chinese IPOs

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ABSTRACT

This paper investigates the relationship between corporate governance mechanisms and cash dividend payment in newly listed firms in China. Using 142 initial public offerings (IPO) listed on the Shenzhen Stock Exchange (SZSE), a dynamic panel Tobit regression is employed. The result shows that large, profitable IPOs with large boards and a high proportion of independent and female directors and CEO duality are willing to pay high dividends to their shareholders. This study indicates the requirement for the promulgation or streamlining of corporate laws in emerging markets to reduce the possibility of expropriation of minority shareholders by politically powered large shareholders.

Keywords : *Corporate governance, Initial Public offerings (IPO), China*

INTRODUCTION

The role of corporate governance in affecting dividend policy has been a subject of interest. Most of the previous research has shown that the patterns of corporate dividend payout policies vary tremendously between developed and emerging markets. This paper investigates the relationship between corporate governance practices and dividend policy in Chinese firms, particularly those which are newly listed.

ARTICLE INFO

Article History:

Received: 05 September 2013

Accepted: 22 March 2014

Published: 30 June 2014

China has been undertaking a series of economic reforms during the past three decades, gradually moving from a centrally planned economy towards a market economy. The formation of the Shanghai Stock Exchange and the Shenzhen Stock Exchange in 1990 was one of the key developments. Besides allowing enterprises to raise funds by issuing corporate bonds and stocks to the public, one of the main tasks for the government is to seek efficiency and productivity transformation in state-owned enterprises (SOEs) through economic and shareholding reforms. The massive privatization of state-owned enterprises in China provides an interesting case study of initial public offerings (IPOs) because of its importance in the transition from socialism to a modern market economy. However, being transformed from SOEs into public firms does not guarantee that the conduct and practices of the governance will be different. Eventually, an ineffective governance system has been widely believed as the root cause of corporate China's lackluster performance. Improving corporate governance is one of the most important tasks of China's continued reform.

To improve corporate governance, the government obviously has an important role to play, for example in strengthening laws that protect shareholder interests and beefing up enforcement of such laws and regulations. Therefore, it is interesting to examine the corporate governance practice in newly listed firms, particularly in affecting dividend policy. There are many reasons this study considers only dividend policy in emerging market IPOs. One is that usually newly listed firms tend to retain their earnings for only a few years after their listing, and consequently firms suffer from free cash flow and expropriation problem; to mitigate these problems good corporate governance is needed. Since it is a new firm operating in an emerging market it is assumed that the corporate governance mechanisms are not fully complied. In addition, investigating the corporate governance impact on dividend policy in emerging markets is significant, because the equity markets in emerging markets are less mature, have information opaqueness and are more volatile.

An IPO occurs when the equity demand of firms can no longer be satisfied by individual or family owners. Then firms can raise capital from outside investors with no existing liquid market. Nevertheless, going public leads to increased potential costs of separation of ownership and control of the firm. Information asymmetry, conflict of interest and free cash flow problems

are highly correlated with separation of ownership and control. Apart from that, there are plenty of opportunities for the controlling shareholders to divert firm resources for individual or family use, because before the IPO stage most of the firms belong to one large individual or family owners. Therefore, firms prefer to pay high dividend as a governance control mechanism that limits corporate insiders' self-serving actions. In 1998, the Organization of Economic Cooperation and Development (OECD) issued its influential *OECD Principles of Corporate Governance*, which are intended to assist member and non-member countries in their efforts to evaluate and improve the legal, institutional and regulatory framework for better corporate governance. Along with that, corporate governance has also gained unparalleled importance in China.

The Chinese government opened stock exchanges in the early 1990s in order to raise capital and improve operating performance for state-owned enterprises (SOEs). By December 2011, one of China's stock markets had emerged as the fifth largest in the world, with market capitalization of over US\$2 trillion. Chinese companies, especially SOEs, have benefited tremendously from the rapid growth in issuance and general public's enthusiasm for the equity market. Nevertheless, the regulations over stock markets have been evolving to address the trade-off between growth and control. The Chinese listed firms suffer from weak protection of minority shareholders and poor corporate governance (Allen, Qian, & Qian, 2005), such as state-owned equity control and conflicts of interests between large dominant shareholders and public shareholders, due to the specific characteristics of the Chinese listed firms. Even though issuance approval, pricing and placement systems have been significantly liberalized, they are still tightly controlled compared to other Asian markets. As controlled as it is, poor governance practices are still rampant among the Chinese listed companies. Moreover, a study of Chinese IPOs is interesting for three main reasons. First, China has experienced large scale IPOs in past years. Second, addressing and understanding the corporate governance impact on emerging market IPOs is both interesting and important because emerging markets' institutional structures are different from those of developed markets. Third, a distinguish feature of Chinese IPOs is that nearly all firms are restructured from state-owned or state-controlled enterprises (Wang, 2004). Hence, a pyramid ownership structure and expropriation is common. After control potential endogeneity, this study finds that

corporate governance is a significant determinant of the dividend policy in Chinese IPOs. In addition, this study provides evidence that agency theory is superior to signalling theory in dividend payment decisions in emerging market IPOs. Overall, this study finds that large profitable IPOs, with large boards and a high proportion of independent directors, pay high dividends to their shareholders. Furthermore, this study finds that boards with a high proportion of female directors and boards where there is CEO duality are willing to pay high dividends to their shareholders.

This study contributes to the literature in several ways. Its findings offer new evidence on corporate governance practices and dividend policy, with particular reference to IPOs in China. Although the IPO phenomenon has caught many researchers' attention, few studies look at the function of corporate governance and IPO firms. Using an extensive dataset on Chinese IPO, this study improves our understanding of the effectiveness of recent corporate governance recommendations in an emerging market IPO context, as well as related practical suggestions for IPOs' governance. Finally, this study controls the endogeneity effect of corporate governance practices in small firms and their dividend-payment, whereas the majority of recent studies have ignored the endogeneity effect of corporate governance, even though some explored the use of the 2SLS regression technique; consequently, the econometric analysis employed in this study is more robust.

The next section reviews prior research and develops the hypotheses, and is followed by discussion of data, variables, methods and procedures used for this empirical study. The results and conclusion then follow.

LITERATURE REVIEW

Dividend policy and the role of dividend announcements has attracted considerable attention in prior literature since the seminal work of Modigliani and Miller (1958). So far there is significant empirical evidence suggesting that management can use the dividend as a signalling mechanism as well as a mechanism to control insider expropriation. Recently, there has been growing literature in both developed and developing markets that has sought to determine the link between dividend policy, firm characteristics and corporate governance practices (Aivazian, Booth, & Cleary, 2003; La-Porta,

Lopez-de-Silanes, Shleifer, & Vishny, 2000). With respect to the dividend policy, the existing literature suggests that firms from developed economies adopt high dividend pay-out policy to decrease agency conflicts between corporate insiders and corporate outsiders. This is because in firms with widespread ownership structure there is conflict between firms' managers and firms' shareholders. Firms in emerging markets tend to pay a high dividend, because it will help to reduce agency conflicts between majority and minority shareholders because closely controlled firms' controlling shareholders often collide with those of the firms' minority shareholders. Corporate governance and dividends in China.

It is generally known that firms that operate in an environment with weak legal protection and institutional settings tend to have less stable dividend policies (Cesari, 2009). Moreover, due to rapid growth of young firms in emerging markets, capital accumulation and expansion leads to restricted dividend payment. Using Chinese listed firms, Shao and Lin (2004) state that fewer dividend initiations and lower dividend payment are prevalent in Chinese market. However, recently the Chinese Securities Regulatory Commission (CSRC) encouraged listed firms to establish long term cash dividend payments through the introduction of new regulatory reforms.

As a first step, CSRC released "Measures for the Administration of the Issuance of Securities by Listed Companies" (2001) and stated that the underwriters of common equity must pay close attention to the refinancing applications by the companies who fail to pay dividends or boards of directors who did not provide justifiable explanations. Furthermore, in 2004, the CSRC stated that if a company had not paid cash dividends in the past three years, firm refinancing will not be approved. Recently, "Measures for the administration of the Issuance of Securities by Listed Companies" (2006) promulgated new rules and indicated that issuance of new shares by Chinese listed companies shall be consistent with the provision that the companies' accumulatively distributed cash or stock dividends over the past three years must be higher than 20% of the average realized annual distributed profits. In addition, the unique ownership structures of Chinese IPOs (where non tradable shares represent more than 60% of outstanding shares) suggest that the cash dividend payment is the primary source of return to the non-tradable shareholders (Chen, Jin, & Xu, 2009; He, Li, Shi, & Twite, 2009). Hence, in recent decades, Chinese listed firms show positive signs of cash dividend pay-outs.

Apart from the above reasons, prior literature suggests corporate governance practices may have significant impact on firm dividend payment (Gugler & Yurtoglu, 2003; Mitton, 2004). Mitton (2004) finds that an increase in a firm corporate governance rating is associated with an average four percentage point increase in dividend payment of emerging market firms. Further, he finds that comparing firms with the worst corporate governance practices and those with the best corporate governance practice, the dividend pay-out ratio for firms with best governance practice is 22 per cent higher than firms with the worst governance practice. This result is consistent with Faccio, Lang and Young (2001), because good corporate governance practices limit expropriation through dividend pay-out.

In the late nineteen hundred's the size and the structure of corporate boards received much attention, fuelled by the financial crisis and business failures of large companies. It was found that board monitoring and controlling activities can increase as more directors are added. However, according to Coles, McWilliams and Sen (2001), large board size increases firm financial performance when a firm operates in a complex environment. Moreover, in the Chinese context, Li and Naughton (2007) find that board size positively impacts on IPO performance. Further, using Chinese listed firms, Howe and Olsen (2006) indicate firms with higher dividend payment ratios have large boards. This may be due to high monitoring activities of large boards' leading to reduced ability to expropriate firm wealth. Similar to corporate governance systems of other East-Asian countries, China's is characterised by the emerging market corporate governance model, which shows highly concentrated equity ownership, pyramided ownership and weak institutional structure. Hence, a large board may increase monitoring activities through increasing a firm's cash pay-out, which constrains corporate insiders' ability to expropriate outsiders, mitigating agency problems.

The independent directors play supervisory and balancing roles, controlling the activities of the executive directors and the board in general. Policy statements, namely the Cadbury Report (1992), the Greenbury Report (1995) and the Hampel Report (1998), emphasise the board monitoring responsibility of independent directors. Independent directors help to ensure managerial accountability of shareholders (Young, 2000). Consequence, increasing trends of independent directors can be observed in last ten years. After introduced CSRC (2001) regulations regarding independent directors

with the objective of introducing better corporate governance practices and protecting the interest of minority shareholders, Chinese firms (through higher pay-out of the dividends) show dramatic increases of independent directors on their boards (Bhabra & Li, 2010; Chen & Zhang, 2002). This is consistent with Howe and Olsen (2006), who find that a higher degree of director independence leads to high performance of Chinese IPOs. This is may be consistent with La-Porta et al's (2000) substitution hypothesis, whereby directors' independence leads to a high dividend pay-out as a substitute for other corporate governance mechanisms of firms.

In recent years, board gender diversity has become the subject of a number of empirical studies. Erhardt, Werbel and Shrader (2003) find that the percentage of female directors is positively related to two accounting measures in larger US firms; return on assets and return on investments. Similar to the above result, Adams and Ferreira (2009) posit gender diversity and firms' financial performance have a significant positive relationship when measured as Tobin's Q and ROA. Therefore, firms with more female directors on their board may have high cash flows, and to reduce free cash flow problems they may pay high dividends to their shareholders. Moreover, boards with a high proportion of female directors may reduce impediments for dividend pay-out. This may be because boards with female directors are inclined to ask many questions and increase board independence (Carter, Simkins, & Simpson, 2003). Therefore, managers cannot use firm cash flow for their own interests.

With the outbreak of large US corporate scandals in early this decade, CEO duality received more attention, due to powerful CEOs abusing their extensive power by expropriating from the company assets and shareholders. Most of the European corporations increased pressure on regulators to separate CEO and chairman roles. Based on the agency theory, Fama and Jensen (1983) suggest that CEO duality hinders a board's ability to monitor management and therefore increases the agency problem. In respect to dividend pay-out, Howe and Olsen (2006) find that one person holding the chairman and CEO positions leads to an increase in the high dividend pay-out ratio. This may be because to reduce expropriation, firms initiate more dividend payments. Furthermore, according to the stewardship theory, the impact of CEO power concentration on firm performance is positive in early stages, and the influence becomes more negative as a firm's life

cycle matures, supporting the agency theory. Therefore, according to the stewardship theory IPOs with CEO duality may prefer to pay more benefits to investors through dividends.

Dividend pay-out policy may become highly important as a monitoring vehicle in profitable firms. Using Polish listed firms, Kowalewski, Stetsyuk and Talavera (2007) find that more profitable firms tend to have a high cash dividend pay-out ratio. This may be because cash dividends coincide with a reduction in the risk of a firm's expropriation. Further, firm size has significant impact on firm dividend policy (Eriotis, 2005; Kowalewski et al, 2007). Eriotis (2005) explains that Greek firms' dividend pay-out ratio is influenced by distributed earnings and size of the firms.

According to the corporate governance mechanisms and dividend pay-out, the hypotheses for this study are formulated as follows:

H₁: IPOs with large board size tend to pay high cash dividends

H₂: IPOs with more independent directors tend to pay high cash dividends

H₃: IPOs with more female directors tend to pay high cash dividends

H₄: IPOs with CEO duality tend to pay high cash dividends

METHODOLOGY

Data and sample selection

The IPOs listed in the Shenzhen Stock Exchange (SZSE) from 2001 to 2005 were collected in this study. The SZSE belongs to 28 major stock exchanges in the world. The majority of SZSE IPOs' applications come from successful high-tech private companies seeking wider share ownership. Data were collected from the Guotaian Research Service Center (GTA_RSC). From the selected period IPO listed only five years, which are 2001-2005. From 2001 to 2005, there was a market slump effect in China, and at this time IPO listed in Chinese stock exchanges significantly decreased compared to economically healthy years. In this time period there were only 142 IPOs listed in SZSE, and without any selection bias this study includes all 142 IPOs. The relevant corporate governance data for each IPO are collected

from Guotaian Research Service Center. After complied dividend pay-out and corporate governance data, approximately above 426 observations create a weakly balanced panel.

Variables

This study includes three dividend pay-out proxies which are highly employed in prior literature. Following Kowalewski et al. (2007) this study used dividend to sales (DIVSAL) and dividend to earnings (DIVEAR) as dividend pay-out proxies and they are calculated as cash dividend to total sales of the IPO and cash dividend to total earnings of the IPO respectively. Following He et al (2009), this study also used dividend to share (DIVSHARE) as proxy for dividend pay-out ratio. It is calculated as cash dividend to total outstanding share.

To find out if corporate governance impacts on dividend pay-out ratio, this study uses board size, independent directors' percentage, female directors' percentage and CEO duality variables as corporate governance explanatory variables. Board size (BSIZE) is calculated as the logarithm of total number of board members. Independent directors' percentage (INDEP) is calculated as the number of independent directors divided by the total number of board directors. Female director percentage (FEMALE) is calculated as the number of female directors divided by the total number of board directors. To capture CEO duality, a CEO duality variable was created. CEO is equal to 1 if CEO duality is present; otherwise, it is set equal to zero.

Apart from the corporate governance variables, this study employed the following control variables as well. The first control variable, firm size (SIZE), is calculated as a natural logarithm of total sales. To capture the year effect this study used 5 year dummy variables representing 2001 to 2005. Furthermore, following Kowalewski et al (2007), this study used ROA and Tobin's Q as explanatory variables of dividend policy. Following Huang and Song (2006), ROA is defined as earnings before interest and tax divided by total assets. This study expects a positive relationship between ROA and dividend payment because ROA reflects the availability of resources to distribute once investment funding is secured, which should increase dividend payment. In this paper, following (McKnight & Weir, 2008), Tobin's Q ratio is defined as market capitalisation plus total debt

divided by total assets. High Tobin's Q is used as proxy for the firm's growth opportunities, hence this study expects negative impact on high Tobin's Q for dividends pay-out ratio.

Panel Tobit regression

Most of the literature uses the Tobit model as an econometric model to describe the relationship between non-negative dependent variables and independent variables. According to Drakos and Bekiris (2010), it is rational to treat board composition, board size and leadership structure as endogenous. This would involve identifying instruments that are variables that are correlated with the key independent variables but that are otherwise uncorrelated with the dependent variable. Therefore, a dynamic panel Tobit model is used as regression analysis to test the relationship between corporate governance factors and firm dividend payment. The cross-sectional non-dynamic Tobit model introduced by Tobin (1958) can be represented as follows.

$$Y_i^* = \beta x_i + \epsilon_i \quad (1)$$

$$Y_i = \max\{Y_i^*, r\}$$

Where Y_i^* is a latent variable, this latent dependent variable has a linear relationship with x_i via a parameter β which determines the relationship between the dependent variable and independent latent variable. Y represents an observed dependent variable, and r is a known constant. The normally distributed error term is denoted by U_i . In a dynamic panel data set, the Tobit model can be explained as follows:

$$Y_{it}^* = x_{it}\beta + y_{it-1}\lambda + \epsilon_{it} \quad (2)$$

$$Y_{it} = \max\{Y_{it}^*, 0\}$$

$$\epsilon_{it} = d_i + u_{it}, \quad t = 1, \dots, T \quad i = 1, \dots, N$$

Model (2) is characterized by lagged latent dependent variables. The component d_i is an unobserved individual specific random disturbance which is constant over time, and u_{it} is an idiosyncratic error which varies across time and individuals. Chang (2002) assumes that d_i and u_{it} are Gaussian conditional x_{i1}, \dots, x_{iT} on. The one common approach for estimating the

dynamic panel Tobit model is the fixed effect. Honore (1993) posits that although a fixed effect Tobit model is valid under weak restrictions on the unobservable heterogeneity, it has major limitations; the model with the time-dummies' variables cannot be estimated consistently. Further, Hu (2003) explains that a dynamic panel Tobit with lagged latent dependent variables and a fixed effects estimator creates more problems. The second possible method for estimating the dynamic panel Tobit model is the random effects approach. By specifying the distribution of the error conditional on the regressors, the random effects estimators can be obtained through maximizing the corresponding likelihood functions (Geweke & Keane, 2000; Lillard & Willis, 1978). A random effects Tobit estimator has the following advantages. First, time-invariant, time-varying, and time-dummies' variables can be incorporated in the model and they can be estimated constantly using the simulation estimator. Secondly, this method allows for complicated dynamic panels, possibly with more than one lag variable. Thirdly, it is a straightforward and easy way to accommodate serial correlations errors (Chang, 2002).

RESULTS

Table 4.1 Descriptive statistics

Variables	obs	mean	Std. Dev	min	max
<i>Depended variables</i>					
Dividend to sales (DIVSAL)	408	.0122918	.0182941	0	.086363
Dividend to earning (DIVEAR)	426	.1102371	.2055344	0	1.5899
Dividend to share (DIVSHARE)	426	.0642723	.0954768	0	.5
<i>Corporate governance variables</i>					
Board size	426	9.438967	2.324758	2	17
Log board size (BSIZE)	426	2.21263	.2619648	.6931472	2.833213
Independent directors (INDEP)	426	.257094	.0404412	0	.75
Female directors (FEMALE)	426	.0120083	.0147563	0	.12

CEO duality (CEO)	426	.8075117	.394718	0	1
<i>Control variables</i>					
ROA (ROA)	426	.0407763	.0582884	-.3903	.2716
Tobin's Q (Q)	426	2.589194	1.615099	.6965	12.8508
Firm size (SIZE)	426	1.95e+09	2.84e+09	2.70e+08	3.00e+10
Y2001	426	.3661972	.4823307	0	1
Y2002	426	.3450704	.4759502	0	1
Y2003	426	.0070423	.0837204	0	1
Y2004	426	.0070423	.0837204	0	1
Y2005	426	.1012191	.1045055	0	.6

Table 4.1 reports descriptive statistics for the sample data. The mean value of the DIVSAL ratio is only 1.2% and it varies between 0% to 8.6% only. Also the mean value of the DIVSHARE variable is low and is indicated at 6.4%. Nevertheless, the mean value of the DIVEAR ratio is comparably higher than DIVSAL and DIVSHARE. However, it is still around 11%. This low dividends payment shows the severity of minority expropriation in Chinese IPOs. This may be caused, according to the La-Porta et al (2000), by countries with weak legal protection for minority shareholders paying lower dividends. Cited by Wei et al (2011), emerging economies increase low dividend payments, non-dividend payments and demonstrate irregular behavior for dividend payments.

Further, Table 4.1 indicates IPO firm board size varies from 2 to 17 members and average board size is 9.4. This average board size of Chinese IPOs is consistent with the recommendations of the European and US codes for ideal board size, being between 5 and 15 members. This study reports that independent directors' mean value is 25% and it varies between 0 to 75%. This indicates that Chinese IPOs still have more inside directors and corporate boards are not independent. Similar to other Asian countries, Chinese IPOs recruited few female board directors on their boards. Table I indicates the mean value of the FEMALE variable is 1.2% and it varies between 0 to 12% only. This finding is consistent with King (2010), and he explains that in China and India women in top companies hold a mere 5 % of board seats. The mean value of non-CEO duality is 80.75%, which indicates that IPOs prefer non-CEO duality in firms. The mean value of ROA is around 0.04. This low ROA may be due to high costs of doing

business in emerging markets. However, mean Tobin's Q value is high and it shows as 2.59 and it varies between 0.7 and 12.9. This high Tobin's Q value indicates IPOs create value for their shareholders.

Table 4.2: Panel Tobit regression results

Variables	DIVSAL	DIVEAR	DIVSHARE
Constant	.0034927 (.0082476)	.1419718* (.0846927)	.0033223 (.0035087)
Corporate governance variables			
Log board size (BSIZE)	.0012466** (.0042388)	.0607173* (.0345393)	-.0049956 (.018016)
Independent directors (INDEP)	.0249315 (.0198452)	.0046832 (.0468937)	.0891565*** (.0284881)
Female directors (FEMALE)	.284268* (.1795981)	.0097156** (.0100094)	-.0073243 (.0050591)
CEO duality (CEO)	.0001809 (.0023478)	.5226394** (.0049863)	.0323774 (.0440987)
<i>Control variables</i>			
ROA (ROA)	.0749268*** (.0169729)	.0661254 (.1533939)	.3462688*** (.0863231)
Tobin's Q (Q)	.0018322*** (.0005304)	-.0096555* (.0056016)	.0034808 (.0032705)
Firm size (SIZE)	2.96-12** (4.12e-12)	1.76e-11*** (4.98e-12)	8.63e-13 (2.18e-12)
Y2001	.0185394 (.0031355)	.1226751 (.0403608)	.0822905 (.0164765)
Y2002	.0111519*** (.0029748)	.0696033** (.0396014)	.0576777*** (.0155615)
Y2003	.0011016* (.0132873)	.289879** (.1854663)	.0249488* (.0684361)
Y2004	.0115901 (.0124867)	-.0669666 (.1780574)	.0485618 (.0646471)
Y2005	-	-	-
No 'of observations	416	416	416
Regression Summary statistics			
Log likelihood	-1237.7091	-1485.547	-1248.675
Chi2	106.23***	156.12***	210.58***

a weakly balanced panel; * Significant at 10% level; **Significant at 5% level; ***Significant at 1%

level; This model provides standard errors which are in parentheses.

Table 4.2 indicates dynamic Tobit regression results of corporate governance and dividend pay-out ratio. Column II reports the relationship of corporate governance and dividend to sales ratio. Column III reports the relationship of corporate governance and dividend to earnings ratio. Finally, Column IV reports the relationship of corporate governance and dividend to share ratio.

Firm board size is found to be correlated with IPO dividend pay-out ratio in previous studies. In Table 4.2, column 2 shows 5% significant positive relationship between dividend to sales ratio and board size, indicating that a large board increases IPO dividend payment. Consistent with the above findings, column 3 indicates 10% significant positive relationship between dividend to earnings ratio and board size as well. One possible explanation for that is when firms have a large board it increases monitoring and distributes firm earnings as dividends to their shareholders. This finding is consistent with Howe and Olsen (2006) and Byoun, Chang and Kim (2012), who find that firms with large boards pay higher dividends to their shareholders. Although independent directors have no significant impact on dividend to sales and dividend to earnings ratios dependent proxies, it is 1% significantly positively related with dividend per share variable, which indicates that independent directors increase the IPO dividend payment ratio. This may be due to independent directors' close monitoring reducing controlling shareholders incentive to siphon resources out of the firms to increase their individual wealth. Hence, free cash flow needs to be distributed among shareholders as dividend. This leads to an increased dividend pay-out ratio of the Chinese IPOs.

Table 4.2 indicates that female board directors are 10% significantly positively related with dividends to sales and dividends to earnings ratios. This finding is consistent with Byoun, Chang and Kim (2012), who find that firms with a high proportion of female directors on their boards are more likely to pay dividends and, further, tend to pay larger dividends than do those with non-female directors on boards. This indicates IPO firms with many female board directors on their board have high dividend pay-out. According to Kandel and Lazear (1992), this may be because gender heterogeneity among board members enhances mutual monitoring and they serve as a "watchdog for shareholders". Accordingly, female board directors have the potential to help align the incentives of managers and shareholders through their impact on the pay-out policy. Additionally, Table

4.2 indicates that the CEO duality variable is 5% significantly positively related with dividend per earnings ratio. However, CEO duality shows a non-significant relationship with dividend per sales and dividend per share proxies. Overall, results indicate that if a single person holds both the CEO and chairman role in a board, IPO leads to paying high dividends. A possible argument for this high dividend pay-out policy is that dividends are used as a signalling device (Battacharya, 1979). Usually, in firms with CEO duality, stakeholders assume firms practice weak corporate governance, and then the positive effect of CEO duality on dividend pay-out policy can be attributed to signalling rather than to monitoring.

Firm performance variables, i.e. ROA and Tobin's Q, are significantly positively related with dividend per share and dividend per earnings, which indicates that high profitability IPOs have high dividend pay-out ratio. This finding is consistent with Naceur, Goaid and Belanes (2007) who find that the highly profitable firms with stable cash flows pay high dividends in Tunisia. This result is also complementary to the findings of Faccio, Lang and Young (2001) who interpret dividends as a method of limiting expropriation of insiders. Nevertheless, Tobin's Q variable is 10% statistically significantly negatively related with dividend per earning variable. This may be because highly profitable IPOs may have high growth opportunities and they reinvest their money, hence the pay-out ratio decreases.

Results indicate that the years 2002 and 2003 are positively related with all three dividend pay-out proxies, which indicates firms tend to pay high dividend in year 2002 and year 2003 compared with other years. This may be due to the CSRC issuing in January 2002 the Code of Corporate Governance of Listed Companies in China; most of the companies inclined to pay dividends to their shareholders. Hence, 2002 and 2003 show a positive impact on dividend payment. However, after the recent financial crisis, that dividend policy tendency of firms in all markets has decline dramatically. Hence, this study finds that after 2003, firm years are not significantly related with dividend proxies.

CONCLUSION AND IMPLICATIONS

This empirical study demonstrates corporate governance is an important determinant in explaining the dividend policy of Chinese newly listed firms. In line with general predictions and controlling for other factors, this study finds that IPOs with large boards and high a proportion of independent directors and female directors are willing to pay a high dividend pay-out. This study's results for the remaining dividend determinants are in line with the corporate finance literature and expectations. Further, this study finds that highly profitable firms with CEO duality also prefer to pay-out their cash flows as dividends. Moreover, it clearly shows that Chinese government corporate governance reforms in 2002 have had a significant influence of dividend payments. However, overall statistics show most of the newly listed Chinese IPOs are reluctant to pay dividends.

A sound legal system in a country helps to protect minority shareholders from majority shareholders' self-dealing behavior, such as excessive compensation, tunnelling and expropriation. Weak investor protection and weak creditor rights in the China market create high expropriation opportunities for closely held firms. De jure and de facto protection for creditors, investors and other related business parties need to be strengthened to avoid expropriation and tunnelling. Therefore, it is necessary to promulgate or streamline the corporate law system in China. Further, there is a need to increase transparency of the recruitment process to achieve the right skills for the company. Good corporate governance practices can improve transparency, accountability and fairness in corporate activities. It is important to have certified managers and directors trained in corporate governance practices. It would help China if it established an institute for corporate governance training. Through capacity building, enforcement and follow-up of corporate governance practices, creating a corporate governance rating system for investors and building up corporate governance awareness among business leaders will improve corporate governance practices in Chinese newly listed companies. A more efficient market with a strong corporate governance system may increase the costs of expropriation and tunnelling among newly listed firms.

LIMITATIONS

Notwithstanding the findings, the current study does have limitations that point to potentially fruitful further research opportunities. First, this empirical result sheds new light on the importance of corporate governance practices, but the current study uses only a few aspects of corporate governance practices. Further studies could consider other corporate governance variables. Second, the findings are based on research in a single country and may not be generalizable. Further studies in both mature and emerging markets will be helpful in terms of international comparability.

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