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Testing of Dividend Signaling Theory

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***Abstract*—This research aims to test whether dividend policy gives positive signal or negative signal to change of company value. The research was conducted at basic industry and chemical company which listed in Indonesia Stoc Exchange period 2006-2015. Variable used in this research is dividend policy in proxy with DPR, and Value Company which in proxy with Tobin's Q. The research method used descriptive and verification methods. Sampling using purposive sampling. The sample size is 10 companies for 10 years with 100 observation data. Statistical analysis used linear regression analysis of panel data. Based on the test results obtained that the dividend policy has a positive effect on the value of the company. The dividend policy provides positive information to investors. Thus the results of the study prove that the dividend policy in the company's basic industrial sectors and chemistry in accordance with dividend signaling theory.**

Keywords—dividend policy; signaling theory; company value

I. INTRODUCTION

The normative goal of a company is to maximize the value of the company or wealth for stockholders [1]. The ups and downs of the company's value can be reflected in the company's stock price in the capital market. For companies that issue shares in the capital market, the traded stock price is an indicator of the company's value [2]. Mursalin et al states the value of public firms showing indicated by the value of all assets and also reflected in the market value [3]. The value of a company is reflected in its stock market price [4].

Dividend signaling theory suggests that increasing dividends will make the market react positively if the market tends to interpret that dividend increases are considered a bright signal about the future prospects of the company, and otherwise the market will react negatively if there is a decrease in dividends perceived as unfavorable signals about future company prospects [5,6]. Petit also added that the announcement of dividends, such as the announcement of dividend payments increased from before, is assessed as a management belief will improve the prospects and performance of companies in the future, and vice versa [7]. Stockholders will interpret the increase in dividend payments made by the company, as a signal that management has predicted high cash flows in the future [8].

The dividend policy is a policy related to the company's decision to divide the revenue generated in the form of dividends to shareholders or hold them as retained earnings for future investment [9]. Dividends can help provide good information about company management to the capital market [10]. Dividends can be viewed as a signal to a company's prospects [11,12]. Companies that have the ability to pay dividends are rated by the public as profitable companies [13].

The dividend policy can be linked to company value. The definition of an optimal dividend policy is a dividend policy that creates a balance between current dividends and future growth so as to maximize the company's stock price [14]. Company value can be affected by dividend policy. Rakhimsah and Barbara stated that the higher the dividend payout ratio, the higher the company's value will be, because the high dividend payout ratio shows the promising dividend payout rate [15]. Gordon's research; Bricley; Bajaj and Vijh resulted that dividends could improve stockholder wealth [16-18]. The results of Ashamu et al and Salawu et al can prove that dividend policy has a positive and significant effect on company value [19,20]. Anton proves that company value is positively influenced by dividend policy, after controlling for the variables of debt, company size, liquidity, and profitability [21]. Miller & Modigliani assuming the perfect market finds that the dividend policy with current corporate value is irrelevant [22]. While the results of Litzenberger & Ramaswamy's research resulted that dividends could decrease the stockholder welfare level [23].

From the above description and research result gap, the researcher is interested to examine the effect of dividend policy on the value of the company in Indonesia, the purpose is to test whether the dividend signaling theory applies not in Indonesia especially to the company of basic and chemical industry sector. The hypothesis proposed that the dividend policy has a positive effect on the value of the company. This research will contribute to companies in Indonesia whether dividend distribution provides a signal or not to investors, and whether the signal is responded positively or negatively, so the company has a basis in making dividend policy so that the policy can increase the value of the company.

II. METHOD

The design used in this research is a causal design that is a useful design to analyze how a variable affects other variables. This research method used with descriptive study with verification method to verify the influence of dividend policy toward company value. Population in this research is company of basic industry and chemical sector which listed in Indonesia

Stoc Exchange period 2006-2015. Sampling research using purposive sampling technique. Based on sampling criteria obtained 25 companies with 83 observation data. The type of data used in the secondary data is panel data. Technique of collecting data using documentation method. Data analysis techniques and hypothesis testing using linear regression analysis of panel data. The selected model approach is common effect model, fixed effect model, and random effect model. Furthermore, to determine the best model using Chow test and Hausman test, followed by regression significance test (F test) and significance test of regression coefficient (T test). Model regresion used in research is $Y = a + bX$.

III. RESULTS

In the panel data regression model has 3 kinds of regression model that is, common effect, fixed effect and random effect. From the results of the three regressions that have been done then to choose which regression model is more appropriate used in this study, it can be done by choosing regression model by using Chow Test and Hausman Test. The results of the Chow Test were performed to determine a more appropriate regression model used between the Common Effects model and the Fixed Effects model, while Hausman's test was performed to determine the more appropriate regression model used between the Fixed Effect model and the Random Effects. The result of choosing the selected model is random effects model with the following result:

TABLE I. DATA PANEL REGRESSION TEST WITH RANDOM EFFECT MODEL APPROACH

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.839880	0.285290	2.943949	0.0040
DPR	1.859330	0.339329	5.479425	0.0000
Cross-section random			0.830323	0.6835
Idiosyncratic random			0.565016	0.3165
	Weighted Statistics			
R-squared	0.231256	Mean dependent var		0.287576
Adjusted R-squared	0.223412	S.D. dependent var		0.647040
S.E. of regression	0.570199	Sum squared resid		31.86247
F-statistic	29.48071	Durbin-Watson stat		1.309301
Prob(F-statistic)	0.000000			

From table 1 it can be seen that the coefficient value is 0.839880 while the coefficient value for the dividend policy variable is 1.859330. So it can be formulated regression equation: Tobin's Q = 0.839880 + 1.859330DPR.

Coefficient value 0.839880 shows that the relationship between independent variables and dependent variable is positive. 0.839880 means that if all independent variables do not change, then the company's value is 0.839880. The dividend policy has a regression coefficient of 1.859330 means that every dividend increase of one percent, it will be followed by the increase of company value of 1.859330 times.

Based on the results of data processing in table 4.1 it can be seen that the value of F arithmetic of 29.48071 and significance of 0.000000 seen that the value of F arithmetic> F table and significance smaller than 0.05 it can be concluded that the regression means. The value of P value of probability 0.0000 is smaller than the specified significance value (0.0000 <0,05) hence the hypothesis accepted, it means dividend policy have positive effect to firm value.

IV. DISCUSSION

Hypothesis testing shows that dividend policy has positive and significant effect. The existence of a significant influence between dividend policy and firm value indicates that changes to dividend policy affect the value of the company, meaning that if the dividend payout (DPR) has increased, then the value of the company will also increase. The results of this study do not support the opinion of Miller and Modigliani which argue that dividend irrelevance policy (dividend irrelevance theory), meaning dividend policy does not affect company value [22].

The results of this study are in line with the Dividend Signaling Theory developed by Bhattacharya stating that the dividend policy as a signal of future prospects [5]. If an increase in dividend will be considered as a positive signal which means the company has good prospects, causing a positive stock price reaction which means the value of the company increases. The results are also in line with the theory of Bird in The Hand proposed by Gordon and Lintner. The Bird in The Hand theory states that the greater the dividend distributed by the company the higher the company's stock price. Gordon and Lintner explained that investors want high dividend payouts because they think that obtaining high dividends is currently less risky than acquiring future capital gains [16,24]. In addition, the results of this study are in line with Bringham which states that managers believe that investors prefer companies that have a stable dividend payout ratio [25]. The dividend distribution will indicate the company earns a large enough profit to distribute it to stockholders. This will increase the market's view of company value.

The results support Bricley's research; Myers & Majluf; Bajaj and Vijh that dividends can improve shareholder wealth [10,18,26]. The results of this study support the research of Ashamu et al and Salawu et al which proves that dividend policy has a positive and significant effect on firm value [19,20]. The results of hypothesis testing in this study indicate that changes in dividend payout ratio increased have a significant influence on stock price changes. Based on signaling theory, the announcement of increasing dividend changes will give a positive signal to investors that impact on the increase in stock prices. Thus the results of this study in accordance with dividend signaling theory.

In Indonesia the dividend distributed to stockholders depends on the outcome of the decision in the General Meeting of Stockholders. However, from the results of this study proves that the company's basic industry and chemicals dividend policy in accordance with dividend signaling theory. Basic industrial and chemical sector companies use dividend policy as a means to send a signal to the market about the future work of the company is the right way, although costly but means for the sustainability of the company. If looking at the financial condition of the company means only a good prospect company that can provide dividends because it has enough cash flow to do so. Thus the market will react to the change in dividends paid, because the market believes that the giver is a successful company. Moreover, if the company gives an increasing dividend every year then many investors are interested to buy shares of the company, so the dividend payout will affect the value of the company.

In this study there are still many limitations, namely the variable under study is only one variable, so for further research it can add other variables that are thought to affect the value of the company in addition to dividend policies such as profitability, company size and liquidity. In addition to this, further research can use moderating variables and control variables. Viewed from the sample, it is only limited to basic industrial and chemical sector companies, so further research can be done on all sectors in the Indonesia Stock Exchange.

V. CONCLUSION

Thus the results of the study prove that the dividend policy in the company's basic industrial sectors and chemistry in accordance with dividend signaling theory.

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