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Dividend Policy and Ownership Structure: Evidence from the Casablanca Stock Exchange

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***Abstract*— This study investigates the effect of the ownership structure on dividend policies for firms listed at the Casablanca stock exchange. Two aspects of the ownership structure are used, the first is the ownership concentration and the second is the identity of the largest shareholders. A panel data analysis is performed to examine the relationship between the dividend policy and the ownership structure in this emerging market for the period between 2004 and 2010. Results show that two forms of ownership identity influence negatively the dividend policy of firms listed. In fact, when the identity of the largest shareholder is either an industrial company or a family, the level of distributed dividends is decreased. Furthermore, findings show that there is no impact of ownership concentration on dividend policies for firms listed at the Casablanca Stock Exchange.**

Keywords-component: Agency Problems, Dividend Policy, Emerging Markets, Ownership Strcuture.

I. INTRODUCTION

Dividend payout decisions have been widely studied in the modern financial literature; they are an important component of the corporate policy. The dividend policy depends on many factors such as the firm's financial performance and liquidity position, its position in its life cycle, taxation and investment opportunities among others. Various dividend policy theories have emerged [1]. Previous studies have investigated the relationship between dividend policy and agency costs. It is shown that the dividend policy diminishes the agency costs that arise from conflicts between the firm's shareholders [2]. If the firm's profits are not distributed as dividends, corporate managers may use them for their own interest and invest in unsuccessful negative NPV projects. Studies about the separation of ownership and control show that the more concentrated the ownership the lower equity agency costs [3].

This paper concentrates on agency theories of dividend policy in an emerging market with a focus on corporate ownership structure and few controlling variables. It provides more insights into the literature by empirically examining the relationship between dividend policy and ownership structure for firms listed in an emerging market where corporate governance mechanics are weak. Findings show that the dividend policy of firms listed in the Casablanca stock exchange is negatively influenced by two forms of ownership identity namely the industrial company and family types of identity. Results also show that there is no impact of ownership concentration on dividend policies.

The remainder of the paper is structured as follows: Section 2 briefly discusses motivation and background for this study, while Section 3 summarizes the data used in the analysis. Section 4 and Section 5 present assessment of our hypothesis and robustness of our results, respectively. The paper ends with Section 6 where we present conclusions.

II. MOTIVATION AND BACKGROUND

Plentiful of prior literature documents inadequacies in corporate governance mechanisms in emerging markets [4]-[6]. This strand of literature considers ineffectiveness of regulatory authorities, weak enforcement mechanisms, and presence of family control as the main reasons behind ineffective governance mechanisms. One of the implications of poor governance mechanisms is exacerbation of agency problems in firms headquartered in emerging markets. Agency problems are supposed to provide means and incentives to insiders to expropriate resources out of firms, thereby adversely affecting firm performance. Mitton (2002) [7], for example, documents poor performance of firms with high agency conflicts. An essential requirement for insiders to expropriate is the extent of control that they exert over firms. This control is, usually, exercised by obtaining controlling stakes in firms. Control of firms allows insiders to expropriate by overpaying themselves, expensing on overambitious projects, undertaking related party transactions, and hiring employees related to them.

Excessive expropriation can lead to reduction in dividend payouts. Prior literature argues that low dividend payout can be an indication of high agency problems [2], [8]. In this paper, we aim to document whether ownership structure of a firm – an important mechanism via which expropriation can take place – affects dividend policies of firms listed at the Casablanca Stock Exchange. For the purpose of this paper, we define ownership structure by two variables: (1) Ownership concentration and (2) Identity of the largest shareholder. Following sub-sections will illustrate how these two variables impact dividend policies in more details.

A. Ownership concentration and dividend policy

Ownership concentration is an internal governance device that allows the largest shareholder to gain control over firm's activities and resources. Such a control, usually, introduces agency conflict between the largest shareholder and the minority shareholders [9]. The agency conflict stems from the fact that ownership concentration provides incentives and

DOI: 10.5176/2010-4804_2.4.259

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means to the largest shareholder to expropriate minority shareholders [10], [11]. Concentrated ownership allows controlling shareholders to conspire with managers to deplete minority shareholders' resources [12]. The expropriation can take a variety of forms. In some instances, the insiders simply steal the profits. In other instances, the insiders sell the output, the assets, or the additional securities in the firm they control to another firm they own at below market prices. Such transfer pricing, asset stripping, and investor dilution, though often legal, have largely the same effect as theft. Furthermore, ownership concentration can also provoke operational inefficiencies when owners are interested in short-term performance rather than long-term profitability [13]. Given the fact that ownership concentration exacerbates agency problems, we argue that it induces controlling shareholders to evade effective disclosure of firm value [14].

In this paper, we argue that ownership concentration, due to its ability to increase agency problems, negatively affects firm performance and leads to lower dividend payout ratios. Our arguments are consistent with previous literature that documents negative relationship between ownership concentration and dividend payout ratios. Mancinelli and Ozkan (2006) [15], for example, examine the relationship between ownership structure and dividend policy for Italian firms and document negative relationship between the voting rights of the largest shareholder and dividend payouts. In another related study, Harada and Nguyen (2011) [16] use a large sample of Japanese firms and show that firms with higher ownership concentration pay lower dividends. This strand of literature argues that ownership concentration affects dividend policies due to its ability to define the extent of agency problems within firms. Firms with concentrated ownership vest more powers in the hands of controlling shareholders, who tend not to disclose all information in order to reap private benefits of control. This paper, therefore, hypothesizes that private benefit of control lead to lower dividend payout ratios.

H1a: Firms with high ownership concentration have low dividends payout ratios

However, plentiful of arguments can be cited to develop a case of a positive relationship between ownership concentration and dividend payout ratios. We argue that insiders of firms with concentrated ownership are aware of the fact that outsiders associate ownership concentration with high agency problems. Therefore, it is in the best interest of these firms to do something that can signal low agency conflicts. We argue that paying high dividends is one such signal. Grossman and Hart (1980) [8] argue that dividend payouts alleviate agency conflicts through the reduction of free cash flow available to managers. In another related study, Jensen (1986) [2] documents that high dividend payouts lessen agency costs by reducing free cash flows that could be expensed on unprofitable projects. This strand of literature argues that paying high dividends reflects managements' good faith and signals low agency problems. Consequently, it is very plausible to assume that firms with ownership concentration pay high dividends.

H1b: Firms with high ownership concentration have high dividend payout ratios

B. Identity of the largest shareholder and dividend policy

This paper argues that identity of the largest shareholder can also provide value relevant information about dividend policies of firms. We believe that every investor has its own motive for amassing control and these motives can significantly affect dividend policies. For the purpose of this paper, we classify the largest shareholders as institutional investor, industrial company, government, family, and foreigner. Prior literature considers institutions as an important channel via which agency problems can be reduced in emerging markets [17]. This strand of literature argues that institutions have greater resources, are more sophisticated, and have more relevant expertise to monitor management. As a result, they are able to force effective disclosure of information [18]-[22]. We argue that low agency problem in firms with institutional investors as the largest shareholder result in high dividend payout ratios. Our conjecture is consistent with Eckbo and Verma (1994) [23] who show that institutional shareholders prefer distribution of dividends in an attempt to reduce agency costs. In another related study, Short, Hao and Kevin (2002) [24] show that dividend payout ratios and the institutional ownership are positively related for the UK firms. Consistent with above literature, this paper hypothesizes high dividend payout ratios for firms with institutional investors as the largest shareholder.

H2: Firms with institutional investor as the largest shareholder have high dividend payout ratios

Industrial company ownership applies when other firms are the largest shareholders of a firm. Prior literature argues that this type of ownership arrangement can positively influence firm performance. Thomsen and Pedersen (2000) [25], for example, assert that the corporate/industrial company ownership ease the transfer of knowledge. They argue that transfer of knowledge enhances the financial performance of a firm and facilitate its growth. In another related study, Williamson (1985) [26] argues that firms end up acquiring shares in others firms in order to monitor managerial discretion. As a result of more monitoring, agency problems are reduced and firm performance goes up. We argue that positive influence of industrial company ownership is, partly, due to the fact that high dividends that may result from better performance can also improve cash flow of industrial company. Therefore, this paper hypothesizes positive impact of industrial company ownership on dividend payout ratios.

H3: Firms with industrial company as the largest shareholder have high dividend payout ratios

In emerging economies, government ownership stems from the lack of property rights [27]. Prior literature associates plentiful of problems with this type of ownership structure [28], [29]. For instance, firms with large government ownership are associated with budget restrictions, absence of innovation, reduced financial performance, and high corruption [30], [31]. In addition, Jen (2007) [32] refers to other problems such as the lack of transparency and the preference of political interests at the expense of economic and strategic benefits in firms with high government ownership. Prior literature shows that these problems translate into poor performance of firms with high government ownership [33]-[36]. Hart, Schleifer and Vishny (1997) [37] show that firms owned by the government

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are more interested in low prices for outputs and higher employment than in profitability. In another related study, Bai, Liu, Lu Song and Zhang (2004) [38] find that when the government ownership is dominant, market valuation is considerably lower. They infer that state intervention lead to bad performance. We argue that bad performance of firms with government ownership translates into low dividend payout ratios.

H4: Firms with government as the largest shareholder have low dividend payout ratios

Family ownership is an important characteristic of firms in emerging markets. Zhang (1998) [39] suggests that family shareholders, particularly when they are also managers, impose significant costs to firm because they may undertake sub-optimal investments due to their lack of diversification. They may hire unskilled family members to managerial positions rather than appointing experienced and qualified executives [40]). When the largest shareholder in a firm is represented by a family, the rights of other shareholders may be abused resulting in poor transparency and absence of accountability [41]. We argue that high agency problems in family controlled firms result in low dividend payout ratios.

H5: Firms with family as the largest shareholder have low dividend payout ratios

Foreign ownership is supposed to positively affect corporate culture and its performance. We argue that having foreigner as the largest shareholder of a firm is a signal that a firm has better governance environment. Our conjecture is based on our assumption that foreigners are trained in appreciating effective corporate governance. Consistent with our arguments, Haniffa and Cooke (2002) [42] report that firms with large proportion of foreign ownership have higher disclosure levels than other firms. In another related study, Khanna and Palepu (1999) [43] show that foreign investors offer monitoring in emerging markets. This strand of literature argues that firms with considerable foreign ownership are able to attract additional local and foreign investors. Their presence, therefore, adds value to the firm. Bai, Lui, Lu, Song and Zhang (2004) [38] document high market value for firms with considerable foreign ownership. In this paper, we argue that lower agency problems and better performance of firms with high foreign ownership translates into high dividend payout ratios.

H6: Firms with foreigner as the largest shareholder have high dividend payout ratio

III. DATA

This paper examines the relationship between ownership structure and dividend polices adopted by firms listed at the Casablanca Stock Exchange during the period between 2004 and 2010. The Casablanca Stock Exchange implemented considerable governance reforms during the past few years. These reforms resulted in arousing considerable interest from investors and enabled the Exchange to more than quadruple during the recent years. Following sub-sections will explain the data in more detail.

A. *Ownership structure*

This paper examines two aspects of ownership structure. The first aspect is the ownership concentration and is measured by Herfindahl index (CONCENTRATION). This index is defined as the sum of the squares of the share of each owner and is between 0 and 1. The higher the Herfindahl index, the higher is the degree of ownership concentration. Concentration of ownership leads to poor information disclosure and higher agency problems [44]). The second aspect of ownership structure is measured via number of dummy variables that differentiate largest shareholders according to their identities. For the purpose of this paper, we divide largest shareholders into five different groups – institutional investor, industrial company, government, family, and foreigner. The institutional investor (INST) is defined by a dummy variable that takes the value of 1 if the largest shareholder is an institutional investor and 0 otherwise. We define institutional investors as banks, insurance companies, pension funds, and mutual funds. The industrial company (IND) is defined by a dummy variable that takes the value of 1 if the largest shareholder is an industrial company and 0 otherwise. The government (GOV) is defined by a dummy variable that takes the value of 1 if the largest shareholder is a state and 0 otherwise. The family (FAM) is defined by a dummy variable that takes the value of 1 if the largest shareholder is a family and 0 otherwise. To identify families, the surnames are used. The foreigner (FOR) is defined by a dummy variable that takes the value of 1 if the largest shareholder is a foreigner and 0 otherwise. All of these groups of investors can affect corporate governance of a firm to varying degrees. Table I documents descriptive statistics for ownership concentration for our sample firms during the period 2004-2010 (Panel A) and across different industries (Panel B). The level of ownership concentration represents on average 35 percent of the structure of the firms in the sample for the different industries analyzed. The maximum level reaches 95 percent. As for the ownership of the largest shareholder, it is shown that 67 percent of the ownership is hold by industrial companies during the sampling period while 6 percent of all firms have the government as the largest shareholder.

Table I: Descriptive statistics for ownership structure variables.

Panel A: Descriptive statistics for ownership concentration for the sample firms during the period 2004-2010.

Variable	Observation	Mean	Standard deviation	Minimum	Maximum
Ownership Concentration	442	0.3569231	0.1823801	0.0316132	0.9513427

Panel B: Descriptive statistics for ownership of the largest shareholder across different industries for the period 2004-2010.

Firms with institutional investors as the largest shareholder (%)	Firms with industrial companies as the largest shareholder (%)	Firms with the government as the largest shareholder (%)	Firms with families as the largest shareholder (%)	Firms with foreigners as the largest shareholder (%)
14.48	66.74	5.66	9.50	6.11

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B. *Dividend policy*

We define dividend policy by the payout ratio (PoR) which is the percentage of earnings paid out as dividends. Dividend payouts are supposed to alleviate agency conflicts through the reduction of free cash flow available to managers. Data for payout ratio was obtained from Worldscope. Table II documents descriptive statistics for payout ratios for our sample firms during the period 2004-2010. The level of distributed dividends represents on average 41 percent for the firms in the sample for the different industries analyzed. The maximum level reaches 100 percent.

Table II: Descriptive statistics for payout ratios for sample firms during the period 2004-2010.

Variable	Observation	Mean	Standard deviation	Minimum	Maximum
PoR	441	40.6539	31.8709	0	100

C. *Control variables*

This paper uses a number of firm-specific characteristics, such as market value (SIZE), total debt to total asset ratio (LEV), and earnings per share (EPS) as control variables. We obtain the data for the above mentioned variables from Worldscope and Thomson Financials. Table III, Panel A, documents descriptive statistics for control variables used in the analysis. The average size of the firms in the sample is 11 million dirhams. As for leverage almost 18 percent of the firms are on average relying on debt in their capital structure. The results in Table III, Panel B, show no severe multicollinearity between our control variables. Therefore, we can include all of the control variables together in our regression equations.

Table III: Descriptive statistics for control variables and correlation matrix of the independent variables. The sampling period is 2004-2010.

Panel A: Descriptive statistics for control variables.

Variable	Observation	Mean	Standard deviation	Minimum	Maximum
Size	396	11.22317	3.878569	3.744267	19.53919
Leverage	201	.1792428	.1877073	0	.877788
Earnings	398	44.60566	49.74834	-48.12778	232.26

Panel B: Correlation matrix of the independent variables.

	Size	**Leverage**	**Earnings**	**instd**	**famd**	**govd**	**fored**	**corpindd**	**herfindhal**
Size	1.0000								
Leverage	0.1539	1.000							
Earnings	-.0641	-0.0328	1.0000						
instd	0.3468	0.1027	-0.0509	1.0000					
famd	-.1873	-0.0041	-0.1783	-.1552	1.0000				
govd	0.2142	0.0068	-0.0748	0.3796	-.0901	1.0000			
fored	0.1139	-0.0955	-0.0694	0.1112	-.0901	-.0524	1.0000		
corpindd	-0.438	-0.0934	0.2049	-.5216	-.5216	-.3030	0.0301	1.0000	
herfindhal	-.0023	0.1122	0.0462	0.1862	-.0831	0.0471	0.1475	0.2123	1.0000

IV. METHODOLOGY

In this section, we document the effect of ownership structure on dividend policy adopted by firms. More specifically, we will look at how different aspects of corporate ownership (that is ownership concentration and identity of the largest shareholder) relate to dividend policy. A panel data analysis is performed in this study and the Hausman test (1978) [45] is performed to find out whether to use fixed effects or random effects while estimating panel data. The Hausman test fundamentally tests the null hypothesis that the individual effects are not correlated with the explanatory variables. The fixed effects model is used if the null hypothesis is rejected since in this case biased estimators will be generated by a random effect model.

A. *Ownership concentration and dividend policy*

Our hypothesis suggests that in concentrated ownership environment, such as Morocco, ownership structure should be the key determinant of dividend policy adopted by firms. In order to test our hypothesis, we estimate a regression with dividend policy (PoR) as a dependent variable and a variable representing ownership concentration (CONCENTRATION) as an independent variable. Given the importance of firm-specific characteristics in determining dividend policy, we add a number of control variables in our regression equation. Consistent with prior literature, we add size (SIZE), leverage (LEV), and earnings per share (EPS) as control variables in our analysis. We also include industry dummies (IDUM) and year dummies (YDUM) in our regression equation. Our regression equation takes the following form.

$$PoR = \alpha + \beta_1 \left(Concentration\right) + \beta_2 \left(Size\right) + \beta 3 \left(LEV\right) + \beta 4 \left(EPS\right) + \sum_{Ind} \beta^{Ind} \left(IDUM\right) + \sum_{Yr} \beta^{Yr} \left(YDUM\right) + \varepsilon \quad (1)$$

The results of the above analysis are reported in Table IV. Results show that neither the concentration ownership nor the added controlling variables (size, leverage and earnings) can explain the level of distributed dividend for firms listed at the Casablanca Stock Exchange.

Table IV: Relationship between ownership concentration and dividend policy.

POR	Coef.
Concentration	-16.18848
Size	-4.420362
Lev	10.57615
EPS	.0468177
Industry Dummies	Yes
Year Dummies	Yes
Number of observations: 200 F-Value: 3.26 R^2 (within): 0.0173	

B. *Ownership identity and dividend policy*

We argued that differences in identities of the largest shareholder can result in differences in dividend policy adopted by firms. In order to test our hypothesis, we estimate a regression with dividend policy (PoR) as a dependent variable and five dummy variables representing ownership identity (FOR, FAM, GOV, INST, IND) as independent variables. As was done before, we add size (SIZE), leverage (LEV), earnings per share (EPS), industry dummies (IDUM) and year dummies (YDUM) as control variables in our analysis. Our regression equation takes the following form.

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$$PoR = \alpha + \beta_1(INST) + \beta_2(IND) + \beta_3(FAM) + \beta_4(GOV) + \beta_5(FOR) + \beta_6(SIZE) + \beta_7(LEV) + \beta_8(EPS) + \sum_{Ind} \beta^{Ind}(IDUM) + \sum_{Yr} \beta^{Yr}(YDUM) + \varepsilon \quad (2)$$

The results of the above analysis are reported in Table V. Our findings show that two forms of ownership identity influence negatively the dividend policy of firms listed at the Casablanca stock exchange for the period 2004 – 2010. In fact, when the identity of the largest shareholder is either an industrial company or a family, the level of distributed dividends is decreased. Industrial company ownership leads to additional monitoring of managerial discretion [26]. In the Moroccan context this may justify the low level of dividends distributed in companies where other firms are among the largest shareholders. As for family ownership, a typical aspect of firms in an emerging market such as Morocco, the low dividend payout ratios are justified by high agency problems in family controlled firms. Family shareholders increase costs for firms because of their lack of diversification [39], the hiring of unskilled family members [40], and the abuse of other shareholders' rights [41]. All this may result in poor transparency and absence of accountability.

Table V: Relationship between ownership identity and dividend policy.

POR	Coef.
INST	dropped
IND	-33.75275**
FAM	-52.8689**
GOV	-48.41492
FOR	9.434468
Size	-9.221982
Lev	12.52178
EPS	0.0593317
Industry Dummies	Yes
Year Dummies	Yes
Number of observations: 200 F-Value: 3.29 R^2 (within): 0.0710	

V. ROBUSTNESS OF RESULTS

In this section, we introduce both set of ownership variables together in a single equation.

$$PoR = \alpha + \beta_1(Concentration) + \beta 2(INST) + \beta 3(IND) + \beta_4(FAM) + \beta_5(GOV) + \beta_6(FOR) + \beta 7(SIZE) + \beta 8(LEV) + \beta 9(EPS) + \sum_{Ind} \beta^{Ind}(IDUM) + \sum_{Yr} \beta^{Yr}(YDUM) + \varepsilon \quad (3)$$

The results of the above analysis are reported in Table VI. Results confirm that firms whose largest shareholder is either an industrial company or a family tend to distribute lower levels of dividends. Findings also report an insignificant coefficient for concentration and for the controlling variables size, leverage and earnings per share. Findings appear consistent with Zhang, 1998 [39]; Perez-Gonzales, 2006 [40] and La Porta, Lopez de Silanes, Schleifer and Vishny, 2000 [41] who document that family ownership is characterized by high agency problems and low dividend payout ratios.

Table VI: Relationship between ownership structure (concentration and identity) and dividend policy.

POR	Coef.
Concentration	74.37823
INST	dropped
IND	-36.18945**
FAM	-60.70656**
GOV	-56.93726
FOR	8.764241
Size	-8.258614
Lev	9.279172
EPS	0.0569318
Industry Dummies	Yes
Year Dummies	Yes
Number of observations: 200 F-Value: 3.26 R^2 (within): 0.0763	

VI. CONCLUSION

This study examines the impact of ownership structure on dividend policies of firms listed at the Casablanca Stock Exchange during the period between 2004 and 2010. Our results show that industrial company ownership and family ownership are the two most important determinants of dividend policies. Consistent with our expectations, we show that family firms distribute lower percentage of earnings as dividends. Unexpectedly, we also show that firms with industrial company ownership also distribute low dividends. Furthermore, we show no impact of ownership concentration on dividend policies for firms listed at the Casablanca Stock Exchange.

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