

**CORPORATE GOVERNANCE IN SIMULTANEOUS MODELLING OF  
CASH HOLDINGS AND LEVERAGE**

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**CORPORATE GOVERNANCE IN SIMULTANEOUS  
MODELING OF CASH HOLDINGS AND LEVERAGE**

By  
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Thesis Submitted to  
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## ABSTRACT

This study investigates the simultaneity of cash holdings and leverage decisions in the presence of ownership and board structures using all listed companies in the Main Market of Bursa Malaysia over a three-year period from 2008 to 2010. Five measures of ownership structures are identified: family, business group, foreign, private domestic institutional investors, government link investment companies (GLICs), and state. Four characteristics of board of directors are specified: board size, board independence, managerial ownership, and CEO duality. The study opted for two stage least squares (2SLS) to estimate the regression models. This is among the earlier studies in Malaysia to consider simultaneity of cash holdings and leverage decisions using 2SLS as an estimation technique. The result showed cash holdings and leverage affect each other negatively. Business group, foreign ownership, board size and CEO duality affect cash holdings and leverage positively while state affects cash holdings and leverage negatively. However, private domestic institutional investors only affect cash holdings positively while GLICs have a positive relationship with leverage. The results did not change when three stage least squares (3SLS) method was used. The major contributions of this study are one, the consideration of both leverage and cash holdings decisions must be done simultaneously and two, policy makers should focus on improving board independence to better protect minority shareholders as this will enhance investors' confidence to invest in a concentrated ownership environment such as Malaysia.

**Keywords:** cash holdings, leverage, ownership structure, board of directors, 2SLS.

## ABSTRAK

Kajian ini meneliti pemilihan keserentakan pegangan tunai dan laveraj terhadap struktur kepemilikan dan lembaga syarikat-syarikat yang tersenarai dalam Pasaran Utama Bursa Malaysia selama tiga tahun dari 2008 hingga 2010. Lima ukuranstruktur kepemilikan telah dikenal pasti: keluarga, kumpulan perniagaan, pemilikan asing, pelabur institusidomestik sektor swasta, syarikat pelaburan berkaitan kerajaan dan pemilikan negeri. Empat ciritadbir urus lembaga pengarah telah ditentukan: saiz, tahap kebebasan, pemilikan pengurusan dan dwi-jawatan ketua pegawai eksekutif. Kajian ini menggunakan Kaedah Kuasa Dua Terkecil Dua Peringkat (2SLS) bagi pengangguran model regresi. Ini merupakan antara kajian terawal di Malaysia yang melibatkan pemilihankeserentakan pegangan tunai dan laveraj menggunakan 2SLS sebagai kaedah penganggaraan. Dapatan kajian menunjukkan pegangan tunai dan laveraj mempunyai hubungan negatif antara satu sama lain. Kumpulan perniagaan, pemilikan asing, saiz lembaga dan dwi-jawatan ketua pegawai eksekutif mempunyai hubungan positif dengan pegangan tunai dan laveraj manakala pemilikan negeri mempunyai hubungan negatif dengan pegangan tunai dan laveraj. Walau bagaimanapun, pelabur institusi domestik sektor swastahanya mempunyai hubungan positif dengan pegangan tunai manakala syarikat pelaburan berkaitan kerajaan hanya mempunyai hubungan positif dengan laveraj. Hasil kajian tidak berubah setelah kaedah Kuasa Dua Terkecil Tiga Peringkat (3SLS) dijalankan. Sumbangan utama kajian ini adalah pertamanya, kedua-dua pemilihan laveraj dan pegangan tunai perlu dipertimbangkan secara seiring, dan keduanya, pihak pembuat dasar perlu lebih fokus dalammenambah baik tahap kebebasan lembaga bagi melindungi pemegang saham minoriti kerana ini akan meningkatkan tahap keyakinan mereka supaya terus melabur dalam persekitaran amalanpemusatan pemilikan seperti Malaysia.

**Kata kunci:** pegangan tunai, laveraj, struktur kepemilikan, lembaga pengarah, 2SLS.

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## **LIST OF ABBREVIATIONS**

CEO	Chief Executive Officer
GLICs	Government-Linked Institutional Investors
OLS	Ordinary Least Squares
SMEs	Small Medium Enterprises
2SLS	Two Stage least Squares
3SLS	Three Stage least Squares
UAE	United Arab Emirates
UK	United Kingdom
US	United States
VIF	Variance Inflation Factor

# **CHAPTER ONE**

## **BACKGROUND OF STUDY**

### **1.0 Introduction**

This chapter starts with background of corporate finance and corporate governance. Section 1.2 examines the problem statement of the study. Section 1.3 identifies the research questions. Section 1.4 determines the research objectives of this study. Section 1.5 examines the scope of the study. Section 1.6 discusses the significance of this study. Section 1.7 presents structure of the thesis.

### **1.1 Background**

Corporate finance and corporate governance are closely related. Corporate finance deals with investment and financing decisions of a firm while corporate governance is concerned with protecting interests of all parties associated with the firm.

#### **1.1.1 Cash Holdings and Leverage Decisions**

In corporate finance, there are three important financial decisions: 1) the capital structure decision (how to acquire the money), 2) the working capital decision (the management of short term assets and liabilities), 3) the capital budgeting decision (where to invest). This study focuses on capital structure (leverage) and working capital (cash holdings).

Cash holdings are one of the major financial decisions made by managers. In occurrence of inflow of cash, a manager must decide whether to distribute the cash

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