THE EFFECT OF FOREIGN OWNERSHIP ON DIVIDEND POLICY: EVIDENCE FROM CHINA

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MASTER OF SCIENCE (FINANCE)

UNIVERSITI UTARA MALAYSIA

MAY 2018

THE EFFECT OF FOREIGN OWNERSHIP ON DIVIDEND POLICY: EVIDENCE FROM CHINA

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Thesis Submitted to
Othman Yeop Abdullah Graduate School of Business,
Universiti Utara Malaysia,
in Partial Fulfillment of the Requirement for the Master of Sciences (Finance)

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ABSTRACT

This study examined the relationship between foreign ownership and dividend policy in the Chinese market. Panel logistic regression was employed to explain the effect of foreign ownership on the choice "to pay" or "not to pay" dividends. Panel model used in this study is constructed by 142 companies' data with 1988 observations involving foreign ownership listed on the Shenzhen Stock Exchange from 2003 to 2016. Findings indicate that a higher level of foreign ownership is associated with a significantly higher probability of paying dividend. This finding is consistent to agency theory and clientele effect theory. The significant positive result for retained earnings to total equity provides support to the implication stated in the life cycle theory. However, the signaling theory is not supported as the results show an insignificant relationship between cash flow and dividend payment, and between investment opportunities and dividend payment. The findings of this study indicates that foreign shareholders in the Chinese market have high preference for dividend paying companies, especially for large companies with low leverage. Hence for investors who prefer dividends, they should invest in companies with foreign ownership as the likelihood of these companies to pay dividend is higher.

Keywords: foreign ownership, dividend policies, panel logistic regression

ABSTRAK

Kajian ini mengkaji hubungan antara pemilikan asing dan polisi dividen di pasaran China. Regresi logistik panel digunakan untuk menjelaskan kesan pemilikan asing ke atas pilihan untuk 'membayar' atau 'tidak membayar' dividen. Model panel yang digunakan dalam kajian ini dibina dengan menggunakan data daripada 142 syarikat dengan jumlah 1988 pemerhatian yang melibatkan pemilikan asing yang tersenarai di Bursa Saham Shenzhen dari tahun 2003 hingga 2016. Keputusan kajian menunjukkan bahawa tahap pemilikan asing yang tinggi berkait rapat secara signifikan dengan kebarangkalian yang tinggi untuk membayar dividen. Penemuan ini adalah konsisten dengan teori agensi dan teori kesan pelanggan. Keputusan signifikan positif bagi perolehan tertahan kepada jumlah ekuiti menyokong implikasi yang dinyatakan dalam teori kitaran hayat. Walau bagaimanapun, teori isyarat tidak disokong kerana keputusan menunjukkan hubungan yang tidak signifikan antara aliran tunai dan pembayaran dividen, dan antara peluang pelaburan dan pembayaran dividen. Keputusan kajian ini menunjukkan bahawa pemegang saham asing di pasaran China lebih mengutamakan syarikat-syarikat yang membayar dividen terutamanya syarikat besar yang mempunyai leveraj yang rendah. Oleh itu, bagi pelabur yang mengutamakan dividen, mereka perlu melabur dalam syarikat yang mempunyai pemilikan asing kerana kemungkinan syarikat ini membayar dividen adalah lebih tinggi.

Kata Kunci: pemilikan asing, polisi dividen, regresi panel logistik

ACKNOWLEDGEMENT

I would like to extend my deepest gratitude and appreciation to my supervisor Prof. Dr. Nur Adiana Hiau Binti Abdullah, a kind and knowledgeable Professor of Universiti Utara Malaysia, for the valuable guidance and constructive comments that led to the completion of this research. I appreciate all your efforts and I consider it a great privilege to do my master program under your guidance.

My deepest gratitude and thanks to my beloved father Yan Pingyu and mother Wang yun, for their love, support and encouragement on my education. It is impossible for me to study oversea without the support of my beloved parents. Your sacrifice is very much appreciated.

Finally, I am highly indebted to all my dear friends who have given me the support in both life and study. Special thanks goes to my roommate: Zhai Runjia. Wang Chen, Pan Jingrui, Pan Ying, Sabirah Sulaiman and all others for their invaluable support, encouragement and real friendship that I needed in UUM and who were there for me all the time. You are more than just friends.

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LIST OF ABBREVIATIONS

Abbreviation	Description of Abbreviation
CSMAR	China Stock Market Accounting Research
CSRC	China Securities Regulatory Commission
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
MM	Miller and Modigliani
OLS	Ordinary Least Square
PCP	Percentage of Correct Predictions
SME	Small and Medium Board
SSE	Shanghai Stock Exchange
ST	Special Treatment
SZSE	Shenzhen Stock Exchange
UK	United Kingdom
US	United States
USD	US Dollar
VIF	Variance Inflation Factor
WTO	World Trade Organization

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

In recent years, rapid development of China's economy has allowed the global population to see the potential of the Chinese market. Stock market plays a critical role in mobilizing savings and investment and this makes it an agent of economic growth and development in any economy. The importance of the stock market in any economy cannot be over emphasized. Compared with other developed countries, China's securities market started relatively late. Since the establishment of the Shanghai Stock Exchange and the Shenzhen Stock Exchange in 1990, after more than 20 years of development, until September 2017, the market capitalization of Shanghai Stock Exchange (SSE) and the Shenzhen Stock Exchange (SZSE) is US$4924 billion and US$3627.4 billion respectively. In terms of world ranking, the Shanghai Stock Excnange and the Shenzhen Stock Exchange ranked fourth and eight places (Shenzhen Stock Exchange Fact Book, 2016).

The development of the securities market over the past ten years is shown in Figure 1.1. The black bar in Panel A of Figure 1.1 shows the aggregate market capitalization of the stock exchanges in China during the period 2006-2015. It increases from RMB8.94billion in 2006 to RMB53.1billion, which is an increase of six times. The gray color bar illustrates the gross domestic product (GDP). GDP presents a year-on-year

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