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The Impact of Bankers on the Board on Corporate Dividend Policy: Evidence from an Emerging Market

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ABSTRACT: This study collects data from Taiwan publicly traded corporations that have banker directors between 2003 and 2007, together with a matching sample consisting of firms without banker directors. Variables used to construct empirical analyses are from the *Taiwan Economic Journal* (TEJ) database. The results indicate that there is a negative relationship between the presence of banker directors and the likelihood of dividend payment. This study contributes to lacuna in the existing banking literature by providing evidence on how banks influence listed corporate dividend policy in emerging markets.

KEY WORDS: banker, board of directors, dividend policy.

Corporate governance has received increasing attention from the business press and community, with a strong emphasis on board monitoring and board independence. The causes and consequences of different corporate governance systems in place all over the world have been the subject of extensive scrutiny in recent years (Gugler 2003).

In Germany and Japan, banks take a more active role in managing financial distress. Further, banks can hold equity stakes in nonfinancial firms, making creditor rights in these countries relatively strong (Kroszner and Strahan 2001).[1] In the United States, regulations restrict the range of financial services that banks can offer and prohibit banks from taking equity stakes in nonfinancial firms (Kroszner and Rajan 1997). Banks can take equity as part of a debt restructuring or bankruptcy workout plan, but they are required to sell their holdings after a specified number of years. In contrast to those countries, although banks in Taiwan can own equity stakes in nonfinancial firms, families widely control firms (Claessens et al. 2002) and are represented on the board of directors. The percentage of firms with bankers on the board in Taiwan is much lower than in Germany, Japan, and the United States, and the bank–commerce affiliation is relatively weaker. Given the relatively scarce bank capital and loose governance in the Taiwan stock market, whether banks can curtail the possibly self-serving behavior of families in such a market is questionable (Lin et al. 2009).

An important financial decision that firms' managers face is the amount and stability of dividends. Miller and Modigliani (1961) argued that dividends are irrelevant in a world with perfect capital markets. Subsequent research discussed the issue of dividends. The finance literature contains several explanations for paying dividends, for example, the

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bird-in-the-hand explanation, the tax-preference theory, and the agency theory.[2] Among these, agency theory is one of the dominant explanations. Prior studies have investigated the association between dividends and corporate characteristics. For example, Jensen et al. (1992) claimed that insider ownership, debt, and dividend policy might relate directly through agency and signaling theories. Gugler (2003) found that target dividend levels, smoothing dividends, and the reluctance to cut dividends depend on the identity of the controlling owner. However, most research focuses on ownership related to dividends. Empirical evidence concerning the link between board-appointed bankers and dividends is limited. Accordingly, this study attempts to complement these findings with bankers on the board.

In East Asia, company ownership is concentrated in the hands of families. Families take an active part in management, with marked separation of control and cash-flow rights. This corporate governance system is a poorly functioning one because of the weak legal protection of small shareholders (La Porta et al. 1999). Therefore, Taiwan presents us with unique opportunities to investigate the role of bank directors in a family-dominated business environment. That is, studying how banks influence listed companies' behaviors through joining the board in the context of an emerging market should extend our understanding of the role of banks for corporate governance in such a market. This study analyzes the role of bankers on the board in relation to firms' financial decisions within the context of the debt models of Byrd and Mizruchi (2005) and Kroszner and Strahan (2001), to understand the role of banker directors in this situation. This investigation conducts further research to continue this line of work, testing the influence of bankers on the board upon firms' dividend policy, as suggested by Byrd and Mizruchi (2005). That is, when banks have some capacity to influence managerial decisions and actions, they can reduce the likelihood of expropriation by family owners. If bankers on the board lead to lower dividends, they can mitigate the principal–principal problem.[3] The empirical results of the study indicate that companies that have banker directors or a greater percentage of banker directors tend not to pay dividends. In addition, as the percentage of banker directors increases, firms pay fewer dividends.

Literature Review and Hypothesis Development

Bankers on the Board

The effects of bankers on the board on corporate policies have been the focus of several theoretical and empirical works in recent years. Firms may gain several benefits by having bankers on their board. For example, bankers on the board may provide management expertise, especially in the form of financial or investment advice (Lorsch and Maclver 1989; Mace 1971). In addition, board-appointed bankers may enhance access to capital by economizing the cost of monitoring (Fama 1985), which in turn may lower the cost of funds (James 1987). Board positions also provide monitoring superiors for loan agreements due to greater information access and the ability to discipline the management through compensation or termination (Kroszner and Strahan 2001). The information advantage afforded by board positions permits better assessment of a firm's creditworthiness to facilitate loans from the represented bank (Fama 1985; Kroszner and Strahan 2001). Finally, bankers on the board may be a form of certification, helping a firm secure capital from other bankers, public debt markets, or investors (Byrd and Mizruchi 2005; Fama 1985).

Some studies have considered that having bankers on the board may lead to conflicts of interest (Kroszner and Strahan 2001). Unlike other outside directors, a banker on the board of a firm has a conflict of interest between the fiduciary duty to a firm's owners and to the bank employer, if the bank is lending to the firm.[4] The different payoff structures associated with debt and equity lead to divergent interests in how each prefers running the firm (Dewatripont and Tirole 1994; Jensen and Meckling 1976). More specifically, shareholders generally prefer higher-risk projects than do lenders because shareholders can capture the upside benefits of risky ventures but are shielded from large losses. This conflict is most intense in firms with very risky investment opportunities and in firms falling into financial distress (Kroszner and Strahan 2001).[5]

Several studies have examined the effect of bank relationships on corporate decisions as well as value. For example, Hoshi et al. (1991) focused on Japanese firms that are members of a *keiretsu*.[6] They argued that this close bank relationship can mitigate information problems that typically arise when debt and equity are diffusely held, and no individual investor has an incentive to monitor the firm. In the case of the United States, Booth and Deli (1999) found evidence that nonlending bankers are associated with higher levels of bank debt, while no significant relationship exists between lending bankers and debt levels. They inferred from these results that nonlending bankers serve on the board as expertise providers, while the role of lending bankers is not clear. Byrd and Mizruchi (2005) suggested two possible explanations for results regarding lending bankers on the board. The first one is that lending bankers may be disabled monitors. The second possibility for the results stems from the limitations of a cross-sectional analysis. Therefore, they examined the three possible role scenarios for bankers on the board: expertise provider, enabled monitor, and disabled monitor. The results suggest that nonlending bankers provide expertise and certification for distressed firms while exercising a monitoring role for nondistressed firms.

Using data from the Spanish market, Gonzalez (2006) suggested that banks make equity investments for both reasons.[7] As banks have incentives to replace equity for debt if agency costs with shareholders increase, the market views bank equity investment concurrent with reductions in bank debt triggered by an increase in these costs. Similarly, because banks only have incentives to lend additional debt to firms if they have positive information about their future prospects, the market infers that bank equity investment concurrent with increases in bank debt are sparked by the banks having insider information on a firm's prospects.

Lin et al. (2009) used detailed information on bank ownership and board composition of Chinese listed companies to understand a bank's decision to own shares of listed companies and the resulting implications for firm performance. They found that companies with banks as leading shareholders witness relatively poor operating performance. Their further analyses indicated that inefficient investment, resulting from bank ownership, are responsible for the disappointing performance. Lai et al. (2008) investigated the motivations and effects of banks to hold equity and participate on the board of their borrowers in Taiwan. Their empirical results reveal that banks are more likely to enter the board of the businesses with higher profitability, higher proportions of tangible assets, and higher public debt ratio in the whole sample for large firms. The results are consistent with the lenders' conflict of interest hypothesis. They also found that in the subsample of small firms, banks tend to be on a smaller board with a higher proportion of liabilities from financial institutions, supporting the agency cost hypothesis.

Overall, banks play an important role in finance by determining the availability and cost of credit. In many countries (e.g., Germany and Japan), banks extend their control and monitor debtors by directly owning company shares and appointing directors (Lin et al. 2009). The existing empirical studies show that the bank relationship has ambiguous effects on corporate decisions and value. Many researchers (e.g., Hoshi et al. 1991) agree that bank ownership provides better capital access to and better monitoring for companies. But some studies (e.g., Lin et al. 2009) suggest that banks do not exercise enough monitoring over their loans.

Dividend Policy

Easterbrook (1984) and Jensen (1986) make an agency theory argument where managers pay dividends to reduce the firm's discretionary free cash flow that could be used to fund suboptimal investments that benefit managers but diminish shareholder wealth.

Using Canadian firms where managers own a large amount of voting stock, Eckbo and Verma (1994) found that cash dividends decrease as the voting power of owner-managers increases, and are almost zero when owner-managers have absolute voting control of the firm. The evidence supports a conflict of interest across various shareholder groups, possibly reflecting a combination of heterogeneous dividend tax rates and managerial preference for free cash flow. Short et al. (2002) also indicate that a positive association exists between dividend payout policy and institutional ownership, while a negative association exists between dividend payout policy and managerial ownership.[8] Iturriaga and Crisostomo (2010) found that dividends play a disciplinary role in firms with fewer growth opportunities by reducing free cash flow under managerial control.

Jensen et al. (1992) examined the determinants of cross-sectional differences in insider ownership, debt, and dividend policy, and found that insider ownership has a negative effect on firms' debt and dividend levels. These results indicate that firms set dividend levels that permit managers to finance expected investment internally. If dividend policy corresponds to managerial projections of future investment opportunities, firms can maintain stable dividends and obtain needed equity financing internally. Myers and Majluf (1984) argued that friction in capital markets leads to competition between dividends and investment projects as potential uses of profits. They showed that firms can build up financial slack by restricting dividends when investment requirements are modest. The cash saved is held as marketable securities or reserve borrowing power.

Farinha (2003) examined the agency theory explanation for the cross-sectional distribution of dividend payout in the U.K. He found a strong U-shaped relationship between dividend payout and insider ownership. He asserted that cash payments to shareholders might help reduce agency problems by increasing the frequency of raising external capital and associated monitoring by investment bankers and investors, or by eliminating free cash flow. Consistent with the agency cost explanation, Gugler (2003) found that in state-controlled firms, smooth dividends have large target payout ratios and are most reluctant to cut dividends, despite the potential costs involved for shareholders. In contrast, family-controlled firms pursue a significantly different dividend policy, showing no smoothing dividends, lower target payout ratios, and reluctance to cut dividends. In addition, they found that firms with low growth opportunities and smooth dividends have larger target payout ratios irrespective of who controls the firm. Lin et al. (2010) also showed that

cash dividend preference is positively related to the proportion of state-owned shares and negatively related to the proportion of tradable shares.

In sum, a number of researchers have also examined the importance that managers and investors attach to dividend policy, and have explained firms' dividend behavior. However, most of these studies involve U.S. data or data from other developed markets, such as the U.K., Canada, and continental Europe, but less research is conducted in emerging markets. In addition, research has neglected the potential relationship between dividend policy and board-appointed bankers. This is especially the case for Taiwanese firms where the ownership structures and institutional framework are different from those of the above-mentioned countries.

The Relationship Between Bankers on the Board and Dividend Policy

While the literature has documented empirical evidence on the relation between dividend policy and management ownership, the potential relationship between dividend policy and the board of directors has been somewhat neglected. The agency cost perspective uses dividends in reducing the agency problem between managers and stockholders. That is, dividend payment reduces the discretionary funds available to managers for perquisite consumption and helps address the manager–stockholder conflict (Easterbrook 1984). In addition to the conflict between stockholders and managers, a similar conflict also exists between stockholders and creditors, since creditors' interests often differ from those of shareholders. Therefore, stockholders may expropriate wealth from creditors by paying themselves dividends. In this situation, creditors may try to contain this problem through restrictions on dividend payment in the bond indenture.

The bank holdup theory suggests that benefits from monitored debts decrease when firm growth prospects improve. If firms' moral hazard problems are severe, banks can monitor and control clients' firms so that monitoring benefits overwhelm costs. When firm quality and growth opportunities improve, the monitoring benefits decrease (Diamond 1991). Rajan (1992) also suggests that such holdup behavior by banks affects firm incentives if banks are unchecked; consequently, firms that have better growth prospects prefer more public debts to monitored debts. In contrast, the information production literature emphasizes that high-growth firms prefer monitored debts to public debts. Yosha (1995) argues that relationship-based financing prevents firms from disclosing proprietary information to product-market competitors, and at the same time, produces positive information for high-growth firms. However, bank holdup theory ignores the fact that growth-based firm valuations tend to hamper the use of public debt, whereas the information production literature ignores the actuality that bank rent extraction especially hurts high growth firms. Wu et al. (2009) point out that funding competition from new equity as an effective natural mechanism solves this concern. Using Japanese data, they show that high-growth firms raise more new equity than do low-growth firms and use more equity relative to bonds in external finance.

Given the profound influence of family block holders on the board composition in Taiwan, internal governance systems are significantly weaker. According to agency theory, large family owners may engage in activities that are in their best interest but not necessarily in the best interest of other shareholders who may not have any voice in the governance of the corporation and only limited formal or informal means to protect their interests. Excess cash flows that would be used for empire building through acquisitions in unrelated areas or in projects of questionable value are returned to shareholders

through dividends, thus reducing agency problems (Yoshikawa and Rasheed 2010). When bankers are appointed to the board, they may serve as firms' monitors to help alleviate agency problems. Thus, firms with bankers on the board may not necessarily pay more dividends to reduce agency costs. The following hypothesis is developed:

> *Hypothesis 1: A banker on the board is negatively associated with the firm's dividend payout.*

Research Methodology

Measuring Dividend Policy ($DP_{i,t}$)

$DP_{i,t}$ represents firms' dividend policy, measured in two ways. Specifically, this study sets the first dividend variable, the dividend dummy ($DP1_{i,t}$), at 1 for firm i in year t if the annual amount of dividends paid is positive, and 0 otherwise. The other dividend variable is the dividend payout ratio ($DP2_{i,t}$), obtained by scaling dividends per share by earnings per share for firm i in year t. For the first measure, we use the logistic regression; for the other measure, we run the ordinary least squares (OLS) test.

Measuring Bankers on the Board ($BC_{i,t}$)

This paper uses two proxies for bankers on the board ($BC_{i,t}$). The first is a dummy variable ($BC1_{i,t}$), which equals 1 if the firm has a banker on its board and 0 if it does not. The second is the number of banker directors divided by the size of the board ($BC2_{i,t}$).

Control Variables

We utilized several controls in our analyses. First, the relationship between growth opportunity and dividend payout is mixed. According to the signaling theory, firms with high levels of growth opportunities face more information asymmetries (Miller and Rock 1985). Therefore, firms with high growth opportunity have incentives to use permanent positive cash flow shocks to increase dividends and signal higher expected earnings. An alternative view to the signaling theory is the agency costs of free cash flow theory. This theory suggests that managers will not invest to maximize shareholder wealth (Jensen 1986). Thus, a dividend increase can limit possible future suboptimal investment, especially for low growth opportunity firms, which have fewer positive net present value (NPV) projects. Furthermore, because growth opportunities are unobservable, many empirical definitions exist. To proxy for growth opportunities, this study uses $MTB_{i,t}$, estimated by the ratio of market value to the book value of assets. This proxy derives from Chung and Pruitt (1994) and is widely used in research as a measure of growth opportunities.

Previous literature has documented the negative effect of leverage on dividend payment. For example, Rozeff (1982) found that firms with higher leverage pay lower dividends to evade the cost of raising firm external capital. Abor and Biekpe (2007) also argued that debt financing is a dominant factor in corporate decisions in some emerging countries. Therefore, we add the debt ratio ($DEBT_{i,t}$) as a control variable, calculated as total debts divided by total assets, and expected to be negatively related to dividends.

Based on the agency theory, institutional shareholders prefer a free cash flow distributed in the form of dividends to reduce the agency costs of free cash flow (Eckbo and Verma 1994). Short et al. (2002) also indicate that institutional shareholders counter

managers' preference for retaining excessive cash flow to force managers to pay out dividends by virtue of their voting power. Following Francis et al. (2005), this study measures institutional ownership ($INST_{i,t}$) as the proportion of common shares owned by domestic investment funds, domestic banks, and foreign investors. The coefficient on $INST_{i,t}$ is expected to be positive.

$SIZE_{i,t}$ is measured by the natural logarithm of total assets. Based on Lloyd et al. (1985) and Vogt (1994), firm size plays a role in explaining the dividend payout ratio of firms. They found that larger firms tend to be more mature and thus have easier access to the capital markets, which reduces their dependence on internally generated funding and allows for higher dividend payout ratios. According to their perspective, this study expects that larger firms offer relatively greater dividends, and thus, a positive sign for $SIZE_{i,t}$.

Yoshikawa and Rasheed (2010) indicate that family owners can exert their influence through their representatives on the board. In addition, family owners pay dividends to minority shareholders. As treating minority owners fairly is more valuable in countries where legal protection for minority shareholders is weak, establishing a reputation for good treatment of minority shareholders will enable these firms to access equity markets in the future (La Porta et al. 2000). Therefore, we use $FD_{i,t}$, measured as the presence of family directors on the board, as a control variable, and expect the coefficient on $FD_{i,t}$ to be positive.

Almeida et al. (2004) argue that higher cash holding generally increases firms' capacity to undertake profitable investment opportunities. Therefore, the interaction variable $BC_{i,t}\_IO_{i,t}$ is included in the model as a control variable to capture the effect of cash flow/investment opportunities on dividend policies of those firms that have bankers on the board, relative to those that do not. We expect a positive coefficient on $BC_{i,t}\_IO_{i,t}$, which implies that dividends increase when the investment opportunities increase in firms with bankers on the board versus firms without bankers on the board.

Finally, in order to control for the industry, exchange, and year effects, we use one industry dummy variable, one exchange dummy variable, and four-year dummy variables.

Empirical Specification

To examine the relationship between bankers on the board and dividend policy, this study uses regression models as follows. We expect that bankers on the board negatively cause dividends. The expected signs for $BC1_{i,t}$ and $BC2_{i,t}$ are therefore negative.

$$\begin{aligned} DP_{i,t} = {} & \beta_o^i + \beta_1 BC1_{i,t} + \beta_2 MTB_{i,t} + \beta_3 DEBT_{i,t} + \beta_4 INST_{i,t} + \beta_5 SIZE_{i,t} + \\ & \beta_6 FD_{i,t} + \beta_7 INDUSTRY_{i,t} + \beta_8 EXCHANGE_{i,t} + \\ & \beta_9 BC_{i,t}\_IO_{i,t} + \sum_{k=2003}^{2006} \beta_t YEAR_t + \varepsilon_{i,t} \end{aligned} \tag{1}$$

$$\begin{aligned} DP_{i,t} = {} & \beta_o^i + \beta_1 BC2_{i,t} + \beta_2 MTB_{i,t} + \beta_3 DEBT_{i,t} + \beta_4 INST_{i,t} + \beta_5 SIZE_{i,t} + \\ & \beta_6 FD_{i,t} + \beta_7 INDUSTRY_{i,t} + \beta_8 EXCHANGE_{i,t} + \beta_9 BC_{i,t}\_IO_{i,t} + \\ & \sum_{k=2003}^{2006} \beta_t YEAR_t + \varepsilon_{i,t}, \end{aligned} \tag{2}$$

where

$Dp_{i,t}$ = dividend policy measures for firm i in year t, including the dividend dummy and dividend payout ratio;

$BC1_{i,t}$ = the bankers on the board dummy, which equals 1 if the firm has a banker on its board in year t, and 0 otherwise;

$BC2_{i,t}$ = the percentage of banker directors for firm i in year t;

$MTB_{i,t}$ = the market-to-book ratio for firm i in year t;

$DEBT_{i,t}$ = the ratio of total debt to total assets for firm i in year t;

$INST_{i,t}$ = the percentage of common shares held by institutional investors;

$SIZE_{i,t}$ = the natural logarithm of total assets for firm i in year t;

$FD_{i,t}$ = the family director dummy, which equals 1 if firm i has one or more family directors on the board, and 0 otherwise;

$INDUSTRY_{i,t}$ = the industry dummy, which equals 1 if firm i belongs to electronics industry, and 0 otherwise;

$EXCHANGE_{i,t}$ = the exchange market dummy, which equals 1 if firm i belongs to the exchange market, and 0 otherwise;

$IO_{i,t}$ = the investment in fixed assets (change in the net fixed assets plus depreciation) dividend by the beginning of the year net fixed asset for firm i in year t; and

$YEAR_t$ = the year dummy, which equals 1 for a specific year, and 0 otherwise.

Sample Selection and Data Source

Sample Selection

This study analyzes all companies listed on the Taiwan Stock Exchange (TSE) and over-the-counter (OTC) stock market over a five-year period from 2003 to 2007.[9] The sample is obtained based on the following criteria:

1. Firms with a fiscal year ending other than the calendar year-end are deleted.
2. In line with other studies (e.g., Peasnell et al. 2005; Vafeas 2005), this study excludes companies in the banking industry because of their substantially different types of corporate investment and accounting data.
3. Firms with substantial events, such as merging, declaring bankruptcy, or being unlisted during the sample period, are excluded.
4. Observations with incomplete data are excluded.

During this sample period, 5,063 observations satisfy these selection criteria. Of these observations, 232 (4.58 percent) are bankers on the board and 4,831 (95.42 percent) are not bankers on the board. The proportion of observations with bankers on the board in Taiwan is rare. Given the limited number of banker directors' observations, this study further adopts the matched-sample approach and identifies two firms without bankers on the board that match each firm with bankers on the board (i.e., on a two-to-one basis) in the same period, in the same industry, and of similar total assets (size).[10] The technique employed helps control the influences of industry and size factors on banker directors. Four observations are eliminated because no suitable match is located.[11] The final sample size comprises 684 observations.[12] The sample selection process is reported in Panel A of Table 1. Panel B lists the frequency of firms with bankers on the board within respective sample years. The number of companies with bankers on the board increases over time, suggesting that banks play a role on the board of directors for firms. Table 2 illustrates the industry distribution of sample companies. The electronics industry firms represent the highest percentage (78.07 percent = 534/684). All but the electronics industry comprise less than 10 percent of the sample firms.

Table 1. Sample details

Panel A: Summary of sample selection procedures

Criteria	Number of obs.
Initial sample	5,499
Less: observations with noncalendar fiscal year-end	10
Observations with banking industry	218
Observations that involved in substantial events	207
Observations with incomplete data	1
Total number of observations	5,063
Dividing into:	
Observations with bankers on the board	232 (4.58%)
Observations without bankers on the board	4,831 (95.42%)
Observations with bankers on the board from 2003 to 2007	232
Less: observations for which no control firm identified	4
Number of observations with bankers on the board	228
Add: Number of observations matched on period, industry and size	456
Final sample	684

Panel B: Frequency of firms with bankers on the board by year

Year	2003	2004	2005	2006	2007	Total
Number of firms	36	43	41	50	58	228
Percentage (%)	15.79	18.86	17.98	21.93	25.44	100.00

Note: Difference between a firm's total assets and its control firms' total assets is greater than 20 percent.

Table 2. Industry distribution of sample firms

	Firms with bankers on the board	Full sample	
Industry	***N***	***N***	**Percentage**
Machinery	7	21	3.07
Chemistry	15	45	6.58
Steel and iron	4	12	1.75
Electronics	178	534	78.07
Construction	2	6	0.88
Transportation	4	12	1.75
Utilities	5	15	2.19
Miscellaneous	13	39	5.70
Total	228	684	100.00

Note: The classification of industries is based on TEJ.

Data Source

All the firm accounting data used to construct empirical analyses are retrieved from the *Taiwan Economic Journal* (TEJ) Finance database. Stock price information is obtained from the TEJ Bank database. Finally, data on banks on the board are collected from the TEJ Company database.

Empirical Results

Descriptive Statistics

Table 3 gives descriptions of the relevant variables along with their mean, standard deviation, first quartile, median, and third quartile. For comparison purposes, we provide descriptive statistics for all firms as well as separately for firms with and without bankers on the board. The means of $DP1_{i,t}$ and $DP2_{i,t}$ for firms with bankers on the board are 0.7368 and 0.5443, respectively, whereas the means of $DP1_{i,t}$ and $DP2_{i,t}$ for firms without bankers on the board are 0.7654 and 0.5756, respectively.

Table 4 presents the correlations among variables. Both $DP1_{i,t}$ and $DP2_{i,t}$ are positively related to $EXCHANGE_{i,t}$ and $BC2_{i,t}\_MTB_{i,t}$. Moreover, $DEBT_{i,t}$ and $INDUSTRY_{i,t}$ is negatively related to $DP1_{i,t}$ and $DP2_{i,t}$. The correlations for all independent variables are below 0.8. The overall results of low intercorrelation among all independent variables indicate that multicollinearity does not appear to be a problem in the regression model. This study subsequently adopts the variance inflation factors (VIFs) to check for potential multicollinearity problems. The VIFs for each independent variable are less than 10. Therefore, no serious multicolinearity exits among the independent variables.[13]

Regression Results

Table 5 presents the regression results of Equation (1) using $DP1_{i,t}$ and $DP2_{i,t}$ as dependent variables.[14] In Panel A, the dependent variable equals 1 if the firm has positive dividend

Table 3. Descriptive statistics

Variables	Mean	Standard deviation	First quartile	Median	Third quartile
Panel A: Descriptive statistics for full firms					
$DP1_{i,t}$	0.7558	0.4299	1.0000	1.0000	1.0000
$DP2_{i,t}$	0.5652	0.4384	0.1565	0.6641	0.7913
$BC1_{i,t}$	0.3333	0.4717	0.0000	0.0000	1.0000
$BC2_{i,t}$	0.0559	0.0907	0.0000	0.0000	0.1215
$MTB_{i,t}$	1.3302	1.1559	0.9149	1.1121	1.4238
$DEBT_{i,t}$	0.3749	0.1534	0.2627	0.3817	0.4757
$INST_{i,t}$	0.1314	0.1480	0.0236	0.0842	0.1873
$ASSET_{i,t}$($thou.)	13,259,655	45,151,537	1,551,524	3,082,260	7,436,355
$FD_{i,t}$	0.8947	0.3071	1.0000	1.0000	1.0000
$INDUSTRY_{i,t}$	0.7807	0.4141	1.0000	1.0000	1.0000
$EXCHANGE_{i,t}$	0.5804	0.4939	0.0000	1.0000	1.0000
$BC1_{i,t}$–$IO_{i,t}$	0.4549	0.9247	0.0000	0.0000	0.9545
$BC2_{i,t}$–$IO_{i,t}$	0.0795	0.2200	0.0000	0.0000	0.1299
Panel B: Descriptive statistics for firms with bankers on the board sample					
$DP1_{i,t}$	0.7368	0.4413	0.0000	1.0000	1.0000
$DP2_{i,t}$	0.5443	0.3830	0.0000	0.6531	0.7953
$BC1_{i,t}$	0.1678	0.0770	0.1146	0.1429	0.2000
$MTB_{i,t}$	1.2935	1.1820	0.9056	1.1060	1.4095
$DEBT_{i,t}$	0.3679	0.1436	0.2683	0.3780	0.4652
$INST_{i,t}$	0.1768	0.1634	0.0549	0.1234	0.2509

$ASSET_{i,t}$($thou.)	13,393,897	45,315,517	1,549,102	3,077,421	7,477,084
$FD_{i,t}$	0.9035	0.2959	1.0000	1.0000	1.0000
$INDUSTRY_{i,t}$	0.7807	0.4147	1.0000	1.0000	1.0000
$EXCHANGE_{i,t}$	0.5482	0.4988	0.0000	1.0000	1.0000
$BC1_{i,t}$–$IO_{i,t}$	1.3646	1.1514	0.9536	1.1398	1.4546
$BC2_{i,t}$–$IO_{i,t}$	0.2386	0.3279	0.1297	0.1700	0.2518
Panel C: Descriptive statistics for firms without bankers on the board sample					
$DP1_{i,t}$	0.7654	0.4242	1.0000	1.0000	1.0000
$DP2_{i,t}$	0.5756	0.4637	0.2948	0.6699	0.7911
$MTB_{i,t}$	1.3485	1.1434	0.9196	1.1165	1.4251
$DEBT_{i,t}$	0.3785	0.1582	0.2588	0.3847	0.4881
$INST_{i,t}$	0.1087	0.1341	0.0114	0.0589	0.1496
$ASSET_{i,t}$($thou.)	13,192,534	45,119,034	1,552,659	3,082,260	7,416,042
$FD_{i,t}$	0.8904	0.3128	1.0000	1.0000	1.0000
$INDUSTRY_{i,t}$	0.7807	0.4142	1.0000	1.0000	1.0000
$EXCHANGE_{i,t}$	0.5965	0.4911	0.0000	1.0000	1.0000

Notes: This table gives descriptions of the research variables along with their mean, standard deviation, first quartile, median, and third quartile. $DP1_{i,t}$ = the dividend dummy, which equals 1 for firms in year t if the annual amount of dividends paid is positive, and 0 otherwise. $DP2_{i,t}$ = dividend payout ratio, which is the ratio of dividend per share to earnings per share for firm i in year t. $BC1_{i,t}$ = the bankers on the board dummy, which equals 1 if the firm has a banker on its board in year t, and 0 otherwise. $BC2_{i,t}$ = the percentage of banker directors for firm i in year t. $MTB_{i,t}$ = the ratio of market value of equity plus book value of debt to the book value of assets for firm i in year t. $DEBT_{i,t}$ = the ratio of total debt to total assets for firm i in year t. $INST_{i,t}$ = the percentage of common shares held by institutional investors. $Asset_{i,t}$= the natural logarithm of total assets for firm i in year t. $FD_{i,t}$ = the family director dummy, which equals one if firm i has one or more family directors on the board, and zero otherwise. $INDUSTRY_{i,t}$ = the industry dummy, which equals 1 if firm i belongs to the electronics industry, and 0 otherwise. $EXCHANGE_{i,t}$ = the exchange market dummy, which equals 1 if firm i belongs to the exchange market, and 0 otherwise. $IO_{i,t}$ = the investment in fixed assets (change in the net fixed assets plus depreciation) dividend by the beginning of the year net fixed asset for firm i in year t. The sample size is 684 observations.

Table 4. Correlation coefficients

Variables	$DP1_{i,t}$	$DP2_{i,t}$	$BC1_{i,t}$	$BC2_{i,t}$	$MTB_{i,t}$	$DEBT_{i,t}$	$INST_{i,t}$	$SIZE_{i}$	$FD_{i,t}$	$INDUSTRY_{i,t}$	$EXCHANGE_{i,t}$	$BC1_{i,t}\_IO_{i,t}$	$BC2_{i,t}\_IO_{i,t}$
$DP1_{i,t}$		0.747***	–0.031	–0.058	0.023	–0.222***	0.092**	0.139***	–0.018	–0.128***	0.213***	0.212***	0.207***
$DP2_{i,t}$	0.733***		–0.007	–0.024	–0.045	–0.179***	0.039	0.055	0.016	–0.175***	0.151***	0.182***	0.178***
$BC1_{i,t}$	–0.031	–0.034		0.974***	–0.015	–0.028	0.259***	0.000	0.020	0.000	–0.046	0.726***	0.726***
$BC2_{i,t}$	–0.084**	–0.065*	0.872***		–0.006	–0.036	0.248***	–0.037	0.021	0.001	–0.066*	0.685***	0.695***
$MTB_{i,t}$	–0.103***	–0.123***	–0.022	0.011		–0.141***	0.078**	–0.133***	–0.091**	0.141***	–0.102***	0.007	0.009
$DEBT_{i,t}$	–0.242***	–0.184***	–0.033	–0.001	–0.135***		0.005	0.195***	0.079*	–0.031	–0.004	–0.063	–0.064
$INST_{i,t}$	0.064*	–0.008	0.217***	0.261***	0.042	0.040		0.350***	–0.032	0.032	0.219***	0.206***	0.205***
$SIZE_{i,}$	0.121***	0.070*	0.000	–0.054	–0.163***	0.177***	0.414***		0.111***	–0.130***	0.590***	0.094**	0.089**
$FD_{i,t}$	–0.018	0.023	0.020	0.032	–0.071*	0.078**	–0.040	0.090**		–0.090**	0.172***	0.044	0.047
$INDUSTRY_{i,t}$	–0.128***	–0.158***	0.000	–0.007	0.115***	–0.049	0.034	–0.074*	–0.090**		–0.193***	–0.021	–0.023
$EXCHANGE_{i,t}$	0.213***	0.172***	–0.046	–0.061	–0.122***	–0.011	0.193***	0.531***	0.172***	–0.193***		0.032	0.029
$BC1_{i,t}\_IO_{i,t}$	0.120***	0.049	0.318***	0.250***	–0.011	–0.045	0.071*	0.015	0.016	0.061	0.009		0.998***
$BC2_{i,t}\_IO_{i,t}$	0.122***	0.065*	0.310***	0.304***	–0.010	–0.037	0.103***	0.015	0.029	0.051	0.019	0.942***	

Notes: This table shows Pearson (in the lower triangle) and Spearman (in the upper triangle) correlation coefficients for variables used in the regression analyses. $DP1_{i,t}$ = the dividend dummy, which equals 1 for firms in year t if the annual amount of dividends paid is positive, and 0 otherwise. $DP2_{i,t}$ = dividend payout ratio, which is the ratio of dividend per share to earnings per share for firm i in year t. $BC1_{i,t}$ = the bankers on the board dummy, which equals 1 if the firm has a banker on its board in year t, and 0 otherwise. $BC2_{i,t}$ = the percentage of banker directors for firm i in year t. $MTB_{i,t}$ = the ratio of market value of equity plus book value of debt to the book value of assets for firm i in year t. $DEBT_{i,t}$ = the ratio of total debt to total assets for firm i in year t. $INST_{i,t}$ = the percentage of common shares held by institutional investors. $FD_{i,t}$ = the family director dummy, which equals 1 if firm i has one or more family directors on the board, and 0 otherwise. $INDUSTRY_{i,t}$ = the industry dummy, which equals 1 if firm i belongs to the electronics industry, and 0 otherwise. $EXCHANGE_{i,t}$ = the exchange market dummy, which equals 1 if firm i belongs to the exchange market, and 0 otherwise. $IO_{i,t}$ = the investment in fixed assets (change in the net fixed assets plus depreciation) dividend by the beginning of the year net fixed asset for firm i in year t. The sample size is 684 observations. *, **, and *** significant at $p < 10$ percent, 5 percent, and 1 percent, respectively, for a two-tailed test.

Table 5. Regression results for Equations 1 and 2

Panel A: Logistic estimates

		Equation (1)			Equation (2)		
Variables	**Predicted sign**	**Coefficient**	**S.E.**	**VIF**	**Coefficient**	**S.E.**	**VIF**
Constant		2.526*	1.515		2.777*	1.529	
$BC1_{i,t}$	–	–0.886***	0.244	1.189			
$BC2_{i,t}$	–				–5.485***	1.352	1.226
$MTB_{i,t}$	?	–0.186**	0.100	1.122	–0.194**	0.102	1.121
$DEBT_{i,t}$	–	–4.654***	0.726	1.097	–4.801***	0.735	1.095
$INST_{i,t}$	+	0.816	0.808	1.347	1.056	0.816	1.405
$SIZE_{i,}$	+	0.230	0.232	1.756	0.206	0.233	1.791
$FD_{i,t}$	+	–0.453	0.347	1.054	–0.409	0.348	1.057
$INDUSTRY_{i,t}$	?	–0.888***	0.283	1.067	–0.910***	0.285	1.067
$EXCHANGE_{i,t}$	?	0.680***	0.240	1.517	0.662***	0.239	1.514
$BC1_{i,t}\_IO_{i,t}$	+	1.121***	0.288	1.123			
$BC2_{i,t}\_IO_{i,t}$	+				5.003***	1.426	1.113
$YEAR_{2003}$	?	–0.117	0.319	1.429	–0.158	0.318	1.427
$YEAR_{2004}$	?	0.271	0.320	1.478	0.261	0.321	1.478
$YEAR_{2005}$	?	–0.042	0.318	1.492	–0.065	0.318	1.495
$YEAR_{2006}$	?	–0.253	0.290	1.468	–0.263	0.292	1.468
Nagelkerke R^2		0.265	0.265				
χ^2		133.838***	133.686***				

(continues)

Table 5. Continued

Panel B: OLS estimates

		Equation (1)			Equation (2)		
Variables	**Predicted sign**	**Coefficient**	**S.E.**	**VIF**	**Coefficient**	**S.E.**	**VIF**
Constant		0.772***	3.264		0.811***	3.402	
$BC1_{i,t}$	–	–0.048	–1.299	1.189			
$BC2_{i,t}$	–				–0.376*	–1.933	1.226
$MTB_{i,t}$	?	–0.040***	–2.723	1.122	–0.040***	–2.717	1.121
$DEBT_{i,t}$	–	–0.599***	–5.486	1.097	–0.590***	–5.420	1.095
$INST_{i,t}$	+	–0.069	–0.548	1.347	–0.045	–0.348	1.405
$SIZE_{i,}$	+	0.021	0.566	1.756	0.015	0.393	1.791
$FD_{i,t}$	+	–0.001	–0.018	1.054	0.001	0.010	1.057
$INDUSTRY_{i,t}$	?	–0.145***	–3.631	1.067	–0.147***	–3.693	1.067
$EXCHANGE_{i,t}$	?	0.108***	2.708	1.517	0.107***	2.696	1.514
$BC1_{i,t}\_IO_{i,t}$	+	0.012	1.579	1.123			
$BC2_{i,t}\_IO_{i,t}$	+				0.106**	2.191	1.113
$YEAR_{2003}$	?	–0.059	–1.131	1.429	–0.061	–1.165	1.427

$YEAR_{2004}$	?	0.017	0.352	1.478	0.017	0.337	1.478
$YEAR_{2005}$	?	0.064	1.266	1.492	0.061	1.211	1.495
$YEAR_{2006}$	?	–0.009	–0.201	1.468	–0.009	–0.190	1.468
D-W		2.077	2.085				
Adjusted R^2		0.090	0.095				
F-statistic		6.208***	6.502***				

Notes: $DP1_{i,t}$ = the dividend dummy, which equals 1 for firms in year *t* if the annual amount of dividends paid is positive, and 0 otherwise. $DP2_{i,t}$ = dividend payout ratio, which is the ratio of dividend per share to earnings per share for firm *i* in year *t*. $BC1_{i,t}$ = the bankers on the board dummy, which equals 1 if the firm has a banker on its board in year *t*, and 0 otherwise. $BC2_{i,t}$ = the percentage of banker directors for firm *i* in year *t*. $MTB_{i,t}$ = the ratio of market value of equity plus book value of debt to the book value of assets for firm *i* in year *t*. $DEBT_{i,t}$ = the ratio of total debt to total assets for firm *i* in year *t*. $INST_{i,t}$ = the percentage of common shares held by institutional investors. $FD_{i,t}$ = the family director dummy, which equals 1 if firm *i* has one or more family directors on the board, and 0 otherwise. $INDUSTRY_{i,t}$ = the industry dummy, which equals 1 if firm *i* belongs to the electronics industry, and 0 otherwise. $EXCHANGE_{i,t}$ = the exchange market dummy, which equals 1 if firm *i* belongs to the exchange market, and 0 otherwise. $IO_{i,t}$ = the investment in fixed assets (change in the net fixed assets plus depreciation) dividend by the beginning of the year net fixed asset for firm *i* in year *t*. The sample size is 684 observations. *, **, and *** significant at $p < 10$ percent, 5 percent, and 1 percent, respectively, for a two-tailed test.

payment, and 0 otherwise. Comparatively, in Panel B, the dependent variable is the dividend payout ratio, measured as dividend per share divided by earnings per share. Therefore, Panel A is the estimation using the logistic regression, while Panel B is the estimation using the OLS specification. Within each panel, this study reports two sets of results. Specifically, this study reports results using the dummy variable of bankers on the board ($BC1_{i,t}$) in column (1) and results using bankers on the board in percentage ($BC2_{i,t}$) in column (2).

In columns (1) and (2) of Panel A, the coefficients on $MTB_{i,t}$ are negative and statistically significant. These results are consistent with the free cash theory. Firms with higher growth opportunities are less likely to pay dividends. The coefficients on $DEBT_{i,t}$ are negative and statistically significant at the 0.01 level. Consistent with earlier studies (e.g., Rozeff 1982), the implication is that high-leveraged firms are less likely to pay dividends. The coefficients on $BC1_{i,t}\_IO_{i,t}$ and $BC2_{i,t}\_IO_{i,t}$ are positive and statistically significant. These findings are consistent with our expectations, indicating a different relationship between cash flow/investment opportunities and dividend policies for firms with bankers on the board. With regard to the main variable, the coefficients on the two measures of bankers on the board ($BC1_{i,t}$ and $BC2_{i,t}$) are negative and statistically significant.

In columns (1) and (2) of Panel B, the coefficients on $MTB_{i,t}$ are significantly negative. These findings indicate that firms with higher growth opportunities are more likely to have a lower dividend payment ratio. Moreover, the coefficients on $DEBT_{i,t}$ are negative and statistically significant at the 0.01 level. The evidence suggests that firms with a higher percentage of debt tend to pay fewer dividends. With regard to the main variable, the coefficient on $BC2_{i,t}$ is significantly negative, while the coefficient on $BC1_{i,t}$ is insignificant.

In summary, the results in Table 5 suggest that the presence of bankers on the board and an increase in the proportion of banker directors influence whether or not firms pay dividends. In addition, the results show that firms with a greater percentage of banker directors are likely to pay fewer dividends.

Sensitivity Analysis

Alternative Measurement of Growth Opportunity

As a robustness check, this paper investigates an alternative growth opportunity metric. Based on Fama and French (1998) and Cheng and Thomas (2006), this study replaces $MTB_{i,t}$ in Equation (1) with the following measurement:

$$ALTMTB_{i,t} = \frac{\text{market value of equity}}{\text{book value of total equity}}.$$

Under the new definition of $MTB_{i,t}$, the predicted signs, significances, and estimated coefficients of independent variables are similar to those in Table 5. Thus, this sensitivity analysis attests to the validity of the original $MTB_{i,t}$.

Alternative Measurement of Dividend Policy

The fact that firms with negative earnings pay dividends may affect the measurement of dividend payout ratio. Therefore, this study further employs dividend yield suggested by Schooley and Barney (1994) to measure dividend policy. Specifically, the denominator of dividend yield is price per share rather than earnings per share. The results are similar to those in Table 5.

Conclusions

Prior literature only explores the impact of banker directors on debt (e.g., Byrd and Mizruchi 2005). This paper addresses whether bankers on the board relate to firms' dividends. Therefore, the empirical analyses of this study extend findings from previous studies. Using a Taiwanese data set, the paper investigates the relationships between bankers on the board and dividend policy. The novelty of this study stems from the characteristics of Taiwanese systems of corporate governance by which insiders dominate boards of directors. In this corporate governance environment with large private benefits of control and concentrated ownership, boards are instruments in the hands of large controlling shareholders.

This study finds evidence that firms with bankers on their boards and a higher percentage of banker directors decrease the probability of dividend payment. The study also indicates that firms with a higher proportion of banker directors have fewer dividend payout ratios. Nevertheless, the results do not show that firms with banker directors are related to dividend payout ratio. Therefore, these findings provide some evidence that bank directors exercise their power to influence corporate dividend policies. More specifically, bankers on the board may mitigate principal–principal conflicts of family-controlled firms.

This paper contributes to the banking literature by providing evidence on how banks influence listed companies' financial decisions in emerging markets. These findings offer new insights into how banks affect listed companies in a setting with weak corporate governance. In addition, this study extends the literature on how the firm–bank relationship affects firms' dividend policy. Byrd and Mizruchi (2005) indicated that the role of bankers on the board might reach beyond debt policy. That is, the extant literature remains controversial as to whether bankers on the board have an impact on dividend policy. These findings from an emerging market add new understandings about related issues. Finally, based on the principal–principal perspective, the results of this study lend some evidence that banks may engage in monitoring. Therefore, we advance the research on family-controlled firms.

This study has several limitations. First, the sample draws from a population of larger firms in unregulated industries. To the extent that governance mechanisms vary across firm size and industry, the results in this study may not be generalizable to smaller firms and firms in regulated industries. Second, the effectiveness of the board's monitoring activities might depend on how the board is structured and organized. This study cannot completely ensure the situation that bankers' role on the board is unique relative to other outside directors. Finally, given our choice of listed Taiwanese firms as our sample, we cannot assume that the results are generalizable to family-controlled firms in East Asian countries. However, as Carney and Gedajlovic point out, restricting the study to one country enables researchers to "hold constant a variety of material contextual considerations" across the entire sample while utilizing "extant sociological, cultural, and historical accounts" of that country (2002, p. 125).

Notes

1. Antimonopoly laws in Germany and Japan limit the percentage of equity that a bank can own in a nonfinancial firm.

2. These studies begin by questioning some of the assumptions that define perfect capital markets analyzed by Miller and Modigliani (1961). The agency cost model views dividends as a tool to manage agency–client conflicts.

3. The problems that arise from conflicts between dominant owners such as family owners and other owners are generally referred to as principal–principal conflicts (Young et al. 2008).

4. Senior creditors, such as banks, prefer the firm to undertake actions that maximize the probability of their repayment rather than maximize the expected return to shareholders. As a result, a banker-director with a material financial interest will not be able to fulfill the functions of a truly independent director (Kroszner and Strahan 2001).

5. Because a banker board position leads to a conflict between banking and fiduciary interests, liability costs may increase for the board-represented bank. Thus, bankers, especially existing lenders, may shun board positions in firms where information asymmetry is high (Byrd and Mizruchi 2005). Kroszner and Strahan (2001) also showed that bank representation on the board is more likely when information asymmetry is low to moderate.

6. A *keiretsu*, or industrial group, coordinates the activities of member firms

7. The Spanish financial system, like the German and Japanese ones, is a bank-oriented system where banks maintain close ties with industrial firms not only by lending them funds but also by taking equity in them.

8. From the tax perspective, there are clear incentives for (tax-exempt) institutions to demand high levels of dividends resulting from the bias in the U.K. tax system in favor of dividends for tax-exempt shareholders. In addition, from the agency perspective, institutions may demand high levels of dividends to force a firm to go to capital for external funding, and hence be subject to monitoring by the external market. Finally, from the free cash-flow perspective, institutions may counter management's tendency to retain excess free cash flow.

9. The year 2007 is chosen as the ending year because of the occurrence of worldwide financial distress in 2008. This crisis resulted in a severe recession and economic deflation. The sample is selected from Taiwan listed companies, and the research period is 2003–7. Because some variables measurements employ data from year $t - 1$ to t, the data collection period covers 2002–7.

10. Prior researchers take equal sample numbers or a two-to-one basis for both groups. However, most literature suggests increasing the numbers of the matching sample. Therefore, this study chooses the two-to-one basis (Beaver 1966; Skogsvik 2005).

11. This paper uses a stricter match on size (e.g., match on assets within ± 20 percent).

12. This study finds that these 228 experimental firms do not affiliate with their banker directors. Our sample shows that a majority of firms with bankers on the board hold one board seat and most banks hold 10–20 percent of board seats for firms with bankers on the board.

13. Gujarati (1995) suggested that multicollinearity is unlikely to be problematic if the VIF is below 10.

14. Outside stockholders response to the dividend announcements depends on investment opportunities and cash flow (Yoon and Starks 1995). Therefore, this study classifies the sample into two categories, high and low investment opportunity, and then tests the mean/median differences in dividend payout ratio between firms with and without bankers on the board. As shown in the following table, we do not observe significant differences in dividend payout ratio across firms with and without bankers on the board.

	Statistics	Firms with bankers on the board	Firms without bankers on the board	*p*-value
High investment opportunity	Mean	0.558	0.512	0.355
	Median	0.042	0.028	0.349
Low investment opportunity	Mean	0.539	0.601	0.172
	Median	0.031	0.028	0.430

Notes: The sample size is 684 observations. *p*-value corresponds to a *t*-test and Wilcoxon nonparametric test (two-sided) for the difference in means and medians between firms with and without bankers on the board.

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