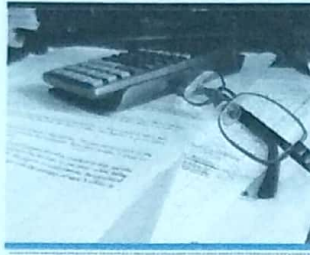


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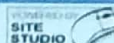
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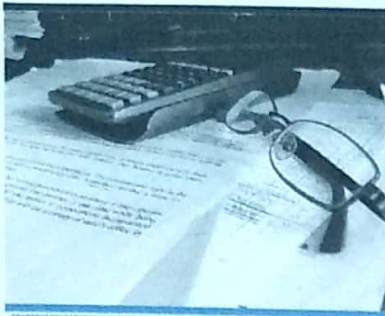
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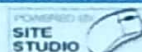
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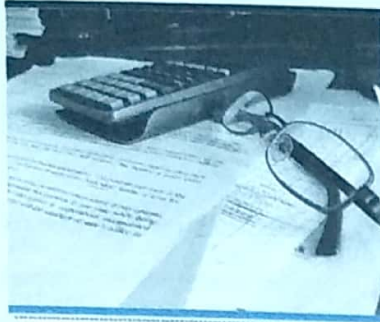
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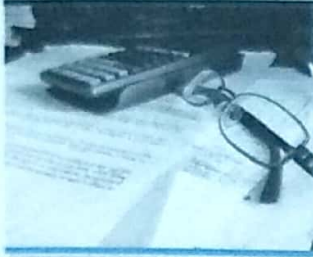
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PUBLICATION CALENDAR

Journal of Academic Research in Economics has a frequency of publication of 3 issues/year. Publication calendar for year 2017:

- Volume 9 Issue 1 - 31 March 2017
- Volume 9 Issue 2 - 31 July 2017
- Volume 9 Issue 3 - 31 December 2017

Authors should send the manuscripts as follows:

- for Volume 7 Issue 1 - until 15 february 2017
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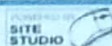
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DETERMINANTS OF CORPORATE CASH HOLDINGS – EVIDENCE FROM INDONESIAN MANUFACTURING COMPANIES

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Abstract

This study is aimed at examining the influence of dividend payments, profitability, liquidity, and firm size for cash holdings in Indonesian manufacturing companies. A total of 32 companies were selected during the observation period between 2010 and 2014 (or 160 observations). Data was analysed by using multiple linear regression. This study found that dividend payments, profitability, liquidity, and firm size both collectively and individually determine cash holdings of the studied manufacturing companies. Therefore, the results are consistent with previous research findings, although it was carry out in a single industry and in a developing country

Keywords: Dividend Payments, Profitability, Liquidity, Firm Size, Cash Holdings.

JEL classification codes: O12, G31

1. INTRODUCTION

There has been growing interest in explaining why firms hold certain and significant amount of cash. According to Gill and Shah (2012), cash holdings refers to cash in the hand or available for invested on assets physical and to be distributed to investors. The benefit and motive behind cash holdings can be easily understood. Some

theories have been used to explain the motivation of cash holdings in companies. For instance, having sufficient cash in hand might reduce the cost of asset liquidation when companies need cash urgently (Anjum and Malik, 2013). But, the determinants of cash holding deserve further investigation because cash holding have opportunity costs (Al-Najjar, 2013). Thus, there has been growing studies in explaining why firms hold cash (Al-Najjar, 2013).

Firms with high cash in hand can exploit profitable project opportunities and pay debt payments in case of cash flow deficits and thus no need to access other financing scheme or sell their assets (Chung et al, 2015). However, higher corporate cash holdings may prove a disadvantage if managers use them for their own benefit at the expense of shareholders. In the other words, cash holdings can be associated with moral hazards as managers do not want to take risks by avoiding investments in potential projects. Consequently, a stock can be downgraded by investors when they detect managers may be hoarding and/or negligently using cash (Kim et al, 2011).

There is a body of literature in cash holdings from developed countries, but not in developing countries (Al-Najjar, 2013). Indeed, researchers have uncovered divergent explanations for the cross-section, cross-country, and time-series variations in corporate cash holdings (Megginson, 2014). We contribute to the literature by examining the determinants of corporate cash holdings in a semi strong market and developing country i.e. Indonesia which has a difference institutional framework. According to their financial report, cash holding of Indonesian manufacturing companies was ranging between 0.21% and 70.19 % of their total assets between 2011 and 2014.

Al-Najjar (2013) believes that that the determinants of cash holdings need to be investigated further because cash holding practice cost every company substantially. While cash holdings have been studied in an array of cross industry firms or in developed countries (Bigelli and Sánchez-Vidal, 2012; Tong, 2011; Subramaniam et al, 2011), we are aware that a limited study targeting cash-holding determinants in a developing countries and in one industry. This study tries to address this gap and encourage further investigation by examining the determinants of cash holdings for these firms. Therefore, the purpose of this study are to testing and analysing the influence of dividend payments, profitability, liquidity, and firm size for cash holdings of manufacturing companies listed in the Indonesia Stock Exchange both collectively and individually.

The rest of this paper is organized as follows. Section 2 formally discusses the theoretical framework and variable definitions used in this paper. Following that, a description of research design is provided in Section 3. Section 4 presents empirical analyses of the effects of dividend payments, profitability, liquidity, and firm size on

their cash holdings. Section 6 concludes and proposes some suggestion for further research.

2. LITERATURE REVIEW

Cash Holdings

Cash holdings in an enterprise can be explained by the theory Keynes (1936) about corporate profits to hold back cash the cost lower transaction and should not be liquidates assets to finance obligations when needed. Arthur, John, William and David (2010: 270) also define cash holdings as currency and coins which is in your company in a drawer petty cash, a cash register, or in of checking accounts and money market.

Among others, three theoretical models have commonly been used to explain cash holdings in previous studies, namely trade-off, free cash flow, and pecking-order theories (Kim et al, 2011). According to trade-off theory proponents suggests that maximizing shareholders oriented management reach an optimal cash-holding level by weighing the marginal benefits and marginal costs of holding cash (Ferreira and Vilela, 2004). Meanwhile, pecking order theory supporters believe that firms prefer internal finance to external finance. Therefore, firms that have higher cash flows are expected to hold larger amounts of cash as are source of internal funds (Ogundipe et al, 2012). Lastly, free cash flow suggests that managers are apt to choose cash because it improves their discretionary power to make investments and acquisitions while simultaneously reducing firm risk (Jensen, 1986).

In cash holdings theory, cash holdings profit for the company according to Keynes (1936): (1) companies can be able to save transaction costs and no need to liquidates the assets if the company need cash; (2) if the source of outside cash financing is really difficult or very expensive; (3) having cash is very useful as a resource of financing, especially when credit crunch occur. Further, Keynes (1936) claimed that there were some benefits to cash holdings based on some motives from a company that does cash holdings among other: transaction motive, precautionary motive, speculative motive and arbitrage motive. Bates et al. (2009) mentioned that there are four main motivations for the firm do cash holdings: transaction motive, precautionary motive, tax motive, and agency motives.

Cash holdings can also be used for other things, namely: (1) be distributed to the shareholders of dividends (Opler et al., 1999; Ozkan and Ozkan, 2004; Al-Najjar and Belghitar, 2011), (2) share repurchases (Soo Lee and Suh, 2011), (3) do investments or keep it for the benefit of companies in the future (Arslan et al., 2006; Ginglinger and Saddour, 2007). According to Ferreira and Vilela (2004) the benefits of cash holdings are: (1) reducing in the likelihood of financial distress, (2) allowing the

pursuance of investment policy when financial constraints were met, and (3) minimizing the costs of raising external funds or liquidating existing assets.

Based on previous literature (Opler et al., 1999; Ozkan & Ozkan, 2004) there are two theories that underlie the companies have cash holdings: trade-off theory and the pecking order theory. Daher (2010) said that explaining cash holdings using three major theories: trade-off theory, pecking order theory, and agency theory.

Dividend Payments

Baridwan (2004:434) stated that the dividend is the portion of profit or advantage distributed to shareholders in the number of comparable to the number of shares owned. Dividends were distributed as part of companies' profits that become the right of a shareholder. Sudana (2011: 24) define dividend pay-out ratio is the ratio that measures how much net profit after a tax is paid as dividends to the shareholders.

Profitability

Profitability is the ability of company deriving profit in connection with sales, total assets and their own capital (Sartono, 2010:122). The profit is reached by company in a particular period is one of the best health factors an enterprise. The shareholders invest to get return over their money (Brigham and Houston, 2013:149).

Liquidity

Liquidity in general can be defined as the level of the ability of an enterprise to be able to pay its debts maturing (Kasmir, 2011:110). Hanafi (2008:77) stated that liquidity also could be defined as a skill of an enterprise meets financial obligations in the short term or that must be paid. Liquidity is also an indicator of company about the ability to pay all financial obligations short-term at maturity using available assets smoothly.

Firm Size

Firm size describes the amount of an enterprise shown by total assets and amount of sales (Sujianto, 2001). Machfoedz (1994) stated that the determination of the size of the company usually is based on total assets company. Further, Machfoedz (1994) explained that the firm size divided into three categories: large firm, medium firm, and small firm.

Thus, hypotheses that tested in this research are follows:

H1: Dividend payment affects cash holdings in manufacturing companies listed in Indonesian Exchange Market

H2: Profitability affects cash holdings in manufacturing companies listed in Indonesian Exchange Market

H3: Liquidity affects cash holdings in manufacturing companies listed in Indonesian Exchange Market

H4: Firm size affects cash holdings in manufacturing companies listed in Indonesian Exchange Market

3. RESEARCH METHOD

This is a hypothesis testing research. This study examines the influence of the independent variable (dividend payments, profitability, liquidity and firm size) for dependent variable (cash holdings). The population of this study consist of manufacturing companies listed in Indonesia Stock Exchange between 2010 and 2014 which published financial statements with accounting year by December 31st and making dividend payments respectively during the observation period years 2010-2014.

The data used in this study is cross-sections data. Cross-sections that is conducted in manufacturing companies listed in Indonesia Stock Exchange that published financial statements with accounting year by December 31st and making dividend payments respectively during the observation period years 2010-2014 are 32 cross-sections or 160 observations.

The data used in this study was secondary data of financial reports and dividends list of a share manufacturing companies from year 2010-2014 obtained through the internet access in the official site of the Indonesian Stock Exchange. Other secondary data used is the theoretical data that supports this study, obtained by means of studies books, journal, articles and other piece of writing.

Cash Holdings (Y)

Cash holdings is a sum of money detained in cash to plans or speculation, deposited or kept at bank, and just gave foreign currencies or securities (Gilarso, 2008:227). Opler et al. (1999) defined that cash holdings is a ratio of the cash with company's assets. Arslan et al. (2006) define cash holdings is the ratio of cash and equivalents to total assets. Size to determine the amount of variable cash holdings in in this research was (Opler et al., 1999; Ozkan dan Ozkan, 2004; Arslan et al., 2006):

$$\text{Cash Holdings} = \frac{\text{Cash and Equivalents}}{\text{Total Assets}}$$

Dividend Payments (X1)

Arthur et al. (2010:201) defined that the ratio of dividend payments is the large of dividends relatively paid to net profit or earnings per share. Al-Najjar (2013) defines

dividend payments is dividend pay-out ratio that is measured by dividend per share divided by earning per share. Therefore, the formula the measurement of dividend pay-out ratio (DPR) is as follows (Husnan, 2008:381; Al-Najjar, 2013):

$$DPR = \frac{\text{Dividend per Share}}{\text{Earning per Share}}$$

Profitability (X2)

Sartono (2010:114) explained that one gauge for indicating the effectiveness of company in producing profit for each asset planted is profitability. In this study, the profitability ratio used is return on equity (ROE), the comparison of earnings after tax as equity shareholders. Al-Najjar (2013) measures the profitability with ROE by comparing earnings after tax as equity shareholders. Profitability can formulate as follows (Sartono, 2010:124; Sudana, 2011:22; Al-Najjar, 2013):

$$ROE = \frac{\text{Earnings after Tax}}{\text{Equity}}$$

Liquidity (X3)

Liquidity is capability of company in satisfying a short term obligation. The liquidity ratio used to measures the company to meet short term liabilities (Van Horne and Wachowicz, 2013:167). The most common liquidity ratios and often used is the current ratio, by summing current assets with total current liabilities company (Sartono, 2010:116). Current ratio (CR) can formulate as follows (Sudana, 2011:21; Van Horne dan Wachowicz, 2013:167; Al-Najjar, 2013):

$$CR = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Firm Size (X4)

Basyaib (2007:122) said that firm size is a scale that can be classified the amount of company according to various ways, such as size income, total assets and in total capital. Firm size is the natural logarithm of total assets (Ozkan and Ozkan, 2004). Al-Najjar (2013) also indicated that firm size is the natural logarithm of total assets. Thus, firm size can formulated as follows (Ozkan dan Ozkan, 2004; Arslan et al., 2006; Kim et al., 2011; Al-Najjar, 2013):

$$SIZE = \ln(\text{Total Assets})$$

The analysis method that used to test hypotheses was multiple linear regression several connecting the independent variable (dividend payments, profitability, liquidity, and firm size with one dependent variable (cash holdings). Data processing was conducted by using SPSS (Statistical Package for Social Science). The analysis methods used in this study were descriptive analysis, the classic assumption testing and

multiple linear regressions. Research methodology used census method, thus there was no significance testing. Hypotheses testing design were done in two steps, the testing design of simultaneously hypotheses and partial hypotheses.

4. FINDINGS AND DISCUSSIONS

The analysis method used in this study were descriptive analysis, the classic assumption testing, multiple linear regression and the hypotheses testing based on the design of the hypotheses testing that had been made. Based on table 1, it is found that cash holdings in the studies companies are highly different.

Table 1: Result of Descriptive Statistic

Items	N	Min.	Max.	Average	Standard Deviation
Cash Holdings	32	0.0245	0.4402	0.1657	0.1291
Dividend Payment	32	0.0868	0.9469	0.4379	0.2429
Profitability	32	0.0340	1.0598	0.2666	0.2175
Liquidity	32	0.7235	7.2624	3.0873	1.8306
Firm size	32	25.462	32.790	28.812	1.7691

Normality test was conducted by seeing significant value at the Shapiro-Wilk of in test of normality table, because the data used in this study is smaller than 50 (or 32 observations). In test of normality table, value significance to shapiro-wilk for all independent variable in this study is greater than 0.05. This shows that the data used in this study is a normal distribution. Moreover, multicollinearity test is conducted by seeing Variance Inflating Factor (VIF) of each variable. Value VIF demonstrate that there is no variable free having the value VIF greater than 10 (1.137 – 1.232). Based on value VIF of each independent variable for which having a value less than 10, so that can be concluded that did not happen multicollinearity between the independent variable in the regression model.

Heteroscedasticity test results performed with use Glejser test shows that regression model was not suffering from a heteroscedasticity, because of the value of significance for all independent variable in this study in Glejser test table greater than 0.05 so does not occur heteroskedasticity symptoms. To test the influence of dividend payments, profitability, liquidity and firm size to cash holdings with simultaneously or partially used the method of multiple linear regressions. The regression equation:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \epsilon$$

$$\ln Y = -7,419 + 0,097 \ln X_1 - 0,030 \ln X_2 + 1,091 \ln X_3 + 1,278 \ln X_4 + \varepsilon$$

Coefficient of determination (R^2) = 0,531

The hypotheses testing undertaken in accordance with a hypothesis that has been formulated. Furthermore, to test hypotheses that had been received then done the testing simultaneously and partially. The results of testing in simultaneously of multiple linear regression shows a value the regression coefficient (β) each variable are: $\beta_1 = 0.097$ for dividend payments variables, $\beta_2 = -0.030$ for profitability variables, $\beta_3 = 1.091$ for liquidity variables and $\beta_4 = 1.278$ for firm size variables.

The determination of hypothesis mentioned that at least one $\beta_i \neq 0$ ($i = 1, 2, 3, 4$), so H_0 accepted, it means simultaneously dividend payments, profitability, liquidity, and firm size an effect on cash holdings in manufacturing companies listed in the Indonesian Stock Exchange. This outcome support first hypotheses (H_1) which was formulated simultaneously dividends payments, profitability, liquidity, and firm size an effect on cash holdings in manufacturing companies listed in the Indonesian Stock Exchange.

The determination coefficients value (R^2) is 0.531 or 53.1 %, this indicates that 53.1 % cash holdings change can be determined by the four independent variable in this study were dividends payments, profitability, liquidity, and firm size, while the rest of 46.9 % was influenced by other variables which were not analysed in this study. The partially testing results on multiple linear regression shows that the regression coefficient each variable are $\beta_1 = 0.097$; $\beta_2 = -0.030$; $\beta_3 = 1.091$ and $\beta_4 = 1.278$. The determination of hypothesis stated that β_i ($i=1,2,3,4$) $\neq 0$ so that H_{a2} , H_{a3} , H_{a4} , and H_{a5} accepted. It means that dividend payments, profitability, liquidity, and firm size have an effect on cash holdings partially in manufacturing companies listed in Indonesia Stock Exchange.

The individual effect of dividend payments on cash holdings in the manufacturing companies listed in Indonesian Stock Exchange is confirmed. The regression coefficient value of 0.097 also indicates that each to raise the dividend payments of 1 % will result in the increase in to cash holdings of 0.097% assuming profitability, liquidity and firm size variables is constant.

The profitability impact on cash holdings is also confirmed in this study. The regression coefficient value of -0.030 also indicates that each to raise the profitability of 1% will result in the decrease in to cash holdings of 0.030% assuming dividend payments, liquidity and firm size variables are constant. The liquidity impact on cash holdings has been found. The regression coefficient value of 1.091 also indicates that each to raise the liquidity of 1% will result in the increase in to cash holdings of 1.091% assuming dividend payments, profitability, and firm size variables are constant. The firm size impact on cash holdings is also documented in this study. The

regression coefficient value of 1.278 also indicates that each to raise the firm size of 1% will result in the increase in to cash holdings of 1.278% assuming dividend payments, profitability, and liquidity variables are constant.

5. DISCUSSION

The regression coefficient value of the independent variables dividend payments, profitability, liquidity, and firm size to cash holdings each of $\beta_1 = 0.097$; $\beta_2 = -0.030$; $\beta_3 = 1.091$; and $\beta_4 = 1.278$. The regression coefficient value indicates that dividend payments, profitability, liquidity, and firm size not equal to zero ($\beta_i \neq 0$; $i = 1, 2, 3, 4$). Thus, simultaneously dividends payments, profitability, liquidity, and firm size an effect on cash holdings in manufacturing companies listed in the Indonesian Stock Exchange. Based on the results of previous hypotheses testing can be concluded that dividend payments had a positive effect on cash holdings. Thus, the bigger dividend payments of a firm are, the larger cash holdings done by the firm, or otherwise.

The result of this study consistent with the results of the study Opler et al. (1999), Drobetz and Gruninger (2007) and Jinkar (2013) who showed that dividend payments had a positive effect on cash holdings. This result is in accordance with statements from that company, which decided to distribute dividends usually back up great cash. This is done to maintain smooth dividend payments and keep liquidity the company remain better after the dividend payments (Jinkar, 2013). Opler et al. (1999) said that the company, which paid dividends, would hold much cash to support the dividend payments.

Based on the results of hypotheses testing, it can be concluded that profitability had a negative effect on cash holdings. This result indicates that the higher profitability a firm would be capable of lowering cash holdings a firm. The result of this study support the results of the study Al-Najjar (2013) in the case of cash holdings in the Brazil, China and United States, as well as the results study Olatunde, Ogundipe and Ajao (2012) who showed that profitability had a negative effect on cash holdings. This result in accordance with statements from that the company to the level of profitability high will do a cash holdings, because cash allocated to short-term investments favourable (Arslan et al., 2006; Ginglinger and Saddour, 2007 and share repurchases (Soo Lee and Suh, 2011).

Based on the results of hypotheses testing, it can be concluded that liquidity had a positive effect on cash holdings. Thus, the bigger liquidity of a firm the larger value cash holdings done by the firm or otherwise. The result of this study consistent with the results of the study Al-Najjar (2013) in the case of cash holdings in the United States that is liquidity have a positive effect on cash holdings. The result in accordance with statements from that the company with a high liquidity will also do cash holdings

a great, to pay all short-term financial liabilities at maturity. This is done to maintain smooth the payment of a short-term financial liabilities and keep liquidity the company remain better after the payment of a short-term financial liabilities (Arthur et al., 2010:272).

Based on the results of hypotheses testing, it can be concluded that firm size had a positive effect on cash holdings. Thus, the large firms are, the larger cash holdings, vice versa. The result of this study support the results of the study Afza and Adnan (2007), Soo Lee and Suh (2011) in the case of cash holdings in Canada, Britain, United States, and study Al-Najjar (2013) in the case of cash holdings in China and United States, which indicates that firm size had a positive effect on cash holdings. This showed that large firms are considered more diversified than their small counterparts are and turn less prone to bankruptcy related costs and hence likely to hold more cash (Al-Najjar and Belghitar, 2011).

5. CONCLUSIONS AND RECOMMENDATIONS

The conclusions of this study are: (1) simultaneously, dividend payments, profitability, liquidity, and firm size had an effect on cash holdings in manufacturing companies listed in the Indonesia Stock Exchange; (2) dividend payments has a positive effect on cash holdings in manufacturing companies listed in the Indonesia Stock Exchange; (3) profitability has a negative effect on cash holdings in manufacturing companies listed in the Indonesia Stock Exchange; (4) liquidity has a positive effect on cash holdings in manufacturing companies listed in the Indonesia Stock Exchange, and (5) firm size has a positive effects on cash holdings in manufacturing companies listed in the Indonesia Stock Exchange.

Recommendations that can be proposed from the study are: further research could be done in all companies registered in Indonesian Stock Exchange that the results of research next can more diversified and conclusions that resulted having the broader that is they did not only on manufacturing companies. Researchers next is also suggested to do testing in test variable other alleged impact on cash holdings as debt, corporate governance, growth opportunities, capital expenditure, net working capital, cash flow, and other financial variables were expected to be affecting on cash holdings company.

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