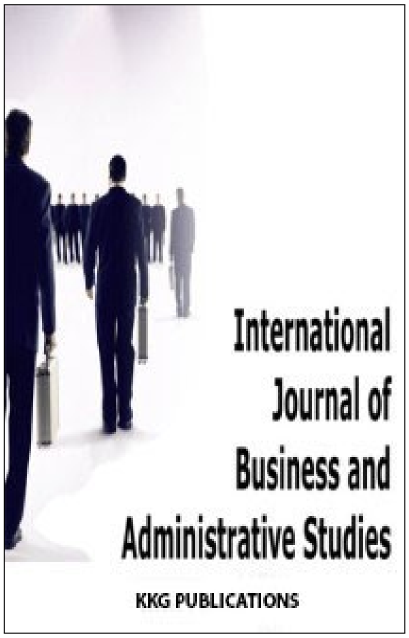

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BOARD SIZE AND DIVIDEND POLICY: A REVIEW

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Abstract. The current study sought to examine theoretical and empirical research on board size and dividend policy. The role of the board has been emphasized in the previous studies in monitoring managerial decisions. In terms of methodology, the current study reviewed and identified the majority of previous research on the role of board size and dividends. The results are mixed regarding the effectiveness of the board depending on its size. The results of the previous studies are mixed, and alternative views are reported based on agency theory and resource dependency theories. Future studies may focus on the composition of boards in terms of their education, knowledge and experience, and board size. The current study is the pioneer study to review the major issues in board size in the dividend policy and relate them to findings of the previous studies on this topic.

INTRODUCTION

Background of Study

One of the central and most debated area in finance is the dividend policy which is still considered a puzzle (Adjaoud & BenAmar, 2010; Bokpin, 2011). Several theories have provided explanations to the dividends, however, none of those have fully explained the theory whereas agency theory have provided the most promising framework (Adjaoud & BenAmar, 2010). Among the role of different corporate governance indicators, the size of board has remained one of the important aspect in previous research (Cheng, 2008; Huang & Wang, 2015; Ning, Davidson, & Wang 2010; Yermack, 1996). Board size is one of the important corporate governance indicator that may help to reduce the agency problem between the shareholders and the management of the company (Hsu & Utami, 2016; Huang & Wang, 2015).

Despite, the very fact that there is no optimal board size, the role of board size is important in most of corporate financial decisions (Huang & Wang, 2015; Yermack, 1996). Since, the power to hire/fire the top management and ratification of other important decisions lies with the board, therefore, role of board is utmost in the firm (Cheng, 2008; Huang & Wang, 2015). Further, the size of the board is one important factor to be considered for the better monitoring function of the board (Huang & Wang, 2015; Ning et al., 2010). The theoretical support to the role of board size in the corporate financial decisions can be traced out from the agency costs and resource dependency theories (Ning et al., 2010).

From the agency cost perspective, size of the board is important because of the monitoring role of the board. Larger boards may not necessarily prove significant in mitigating agency conflicts because large board members will try to satisfy large number of clienteles. Larger boards have lower coordination and processing skills (Hackman, 1990) because more members in the board may lower the quality of the decisions (Jensen, 1993; Yermack, 1996). Since, the coordination among the members of the large boards is less there monitoring role is less efficient and therefore smaller boards are able to perform the governance function in a better way (Jensen, 1993). For instance, Bradford, Chen, and Zhu (2013); Sundar and Al-Harthi (2015) reported positive impact of board size on the cash dividends which implies that larger boards are less efficient thereby increases the cash dividends.

The companies with this type of board will also pay higher dividends because large board members will try to satisfy variety of shareholders (Yarram & Dollery, 2015). This argument supports the substitution hypothesis because dividends in this case may serve as alternative governance mechanism (La Porta, Lopez-de-Silane, Shleifer, & Vishny, 2000). According to Yarram and Dollery (2015), board size is positively related to the dividend payout. Similarly, other studies also reported that board size has significant positive relationship with the dividend payout (Abor & Fiador, 2013; Bokpin, 2011; Jiraporn & Ning, 2006; Nuhu, Musah, & Senyo, 2014). Most recently, Chen, Leung, and Goergen (2017) reported positive impact of board size on the dividend pay-out. Likewise, Saeed and Sameer (2017) reported

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that dividend and board size are positively related.

In contrast, Ning et al. (2010) stated that firms with smaller board try to increase the size to the optimal level and refer it to the resource dependency theory. Further, they argue that firms with larger boards decreases the size of the board to bring it to the optimal level. According to their study, the decrease in the size of the board will decrease the free ridings problems and refer it to the agency theory. Based on these arguments, two alternative views may be drawn. First is based on the agency theory which states that larger boards are weak in monitoring therefore firms pay high dividends as an alternative governance mechanism. Second view is based on the resource dependency theory which states that larger boards are better in monitoring because of more diversity and skills involved by large member therefore there is no need to pay high dividends as alternative governance mechanism.

Since, larger boards entails more experts therefore more experience, skills and diversity can increase the monitoring role of the board (Klein, 2002; Ning et al., 2010). Many previous studies have reported negative relationship of board size with the dividends (Alias, Rahim, Nor, & Yaacob, 2012; Batool & Javid, 2014; Endang & Risal, 2017; Ghosh & Sirmans, 2006; Hosban, 2016; Rehman, Hasan, Mangla, & Sultana, 2012). Klein (2002) stated that increase in board size may increase the monitoring function of the board and will enhance the effectiveness. The increased monitoring by the larger boards reduces the dividend payout because increased monitoring supports the monitoring hypothesis. Furthermore, the increased monitoring by the larger boards decreases the need for dividends as substitute governance mechanism. According to La Porta et al. (2000) smaller boards may or may not pay higher dividends in that when they try to make the reputation in the market they will start paying higher dividends.

Setia-Atmaja, Tanewski, and Skully (2009) found no significant impact of board size on the dividend decision. Brown and Caylor (2004) reported that those firms that have a board size of minimum six directors and maximum fifteen directors enjoys high return on equity and profits as compared to the others.

The current study is the pioneer study to review the major issues in the role of board size in the dividend policy and relate them to findings of the previous studies on this topic. Moreover, the findings of previous studies are briefly reviewed based on the primary theories related to the board size and dividend policy. Most of the review studies have a major limitation in that while review some of the studies are left out. Correspondingly, the publication of new studies on any topic make the previous review studies outdated (Bhattacharyya, 2007) and it and demands for recent review studies. Thus, the current study has focused on the board size and dividends by considering the most recent studies on this topic.

METHODOLOGY OF STUDY

The current study has conducted a review of the theoretical and empirical studies regarding the role of board size in dividend payouts. The review and empirical studies on this topic are identified and reviewed. Furthermore, the findings of those studies are discussed based on the agency and resource dependency theories. Following section elaborates the findings of previous research on the role of board size in the dividends.

Board Size and Dividends

The relationship between board features like independence and size and performance is a central topic in the corporate governance area (Cheng, 2008). The board size is relevant to the value of firm because value of firm is related to the effectiveness of the board (Yermack, 1996). Prior studies have documented the effect of different corporate governance indicators on the dividends (Abor & Fiador, 2013; Batool & Javid, 2014; Benjamin & Zain, 2015; Bokpin, 2011; Gugler & Yurtoglu, 2003; Mehdi, Sahut, & Teulon, 2017; Mitton, 2004) whereas the literature about board size is thin.

The relationship between board size and dividends can be explained based on the outcome and substitution hypothesis of La Porta et al. (2000). Since, outcome hypothesis states that dividends are the outcome of better governance practices. Based on this view, the firms may pay high dividends with better governance structure. However, it seems difficult to interpret whether larger boards reflect better monitoring because the results on board size and performance are also mixed. However, overall agency perspective states that larger boards entails more directors in the board which reduces the coordination among them (Hackman, 1990) therefore firms with large board size may pay high dividend as substitute governance mechanism consistent with the substitution hypothesis of La Porta et al. (2000). Many previous studies has reported positive impact of board size on dividends in different countries such as Ghana (Abor & Fiador, 2013), Australia (Yarram & Dollery, 2015), USA (Jiraporn & Ning, 2006), Russia (Saeed & Sameer, 2017), China (Bradford et al., 2013; Saeed & Sameer, 2017), India (Saeed & Sameer, 2017).

Instead, of agency theory, resource dependency theory presents a different view. The relationship between boards size and dividends might be explained in an alternative manner. Based on the resource based theory, the larger boards might be more effective monitoring tool by having more skills, knowledge and diversity. The increased monitoring by the board can reduces the dividends because effective monitoring can reduce the need for dividends as alternative governance mechanism. Given the theoretical support, the previous studies have documented negative impact of board size on the dividends in different countries such as Pakistan (Batool & Javid, 2014; Rehman et al., 2012), Malaysia (Alias et al., 2012) and USA (Ghosh, 2006).

TABLE 1
Board Size and Dividend

Sr. No.	Author	Country	Data	Findings
1	Bokpin (2011)	Ghana	2002-2007	Positive relationship
2	Yarram and Dollery (2015)	Australia	2004-2009	Positive relationship
3	Abor and Fiador (2013)	Sub-Saharan Africa	1997-2006	Positive relationship
4	Jiraporn and Ning (2006)	USA	1993,1995,1998-2000, 2002	Positive relationship
5	Chen et al. (2017)	USA	1997-2011	Positive relationship
6	Saeed and Sameer (2017)	India, China, Russia	2007-2014	Positive relationship
7	Bradford et al. (2013)	China	1999-2010	Positive relationship
8	Rehman et al. (2012)	Pakistan	1998-2008	Negative relationship
9	Alias et al. (2012)	Malaysia	2002-2007	Negative relationship
10	Batool and Javid (2014)	Pakistan	2003-2011	Negative relationship
11	Ghosh and Sirmans (2006)	USA	1999-2000	Negative relationship

CONCLUSION

The current study has reviewed the main theoretical and empirical studies examining the role of board size in the dividend pay-outs. The findings of these studies have highlighted many theoretical and practical issues pertaining to the role of board size in the dividend policy. The current study provides complete understanding of the effectiveness of board size in corporate financial decision making. Furthermore, the current study provides the reader the key facts on the role of board size in dividend policy.

However, these findings have provided the mixed results. Since, the findings are inconclusive providing alternative theoretical support, future research may focus on the experience, diversity, education and skills in board along with the size of the board. Despite some inconclusive evidence about the role of board size in paying dividends, our review highlights that some explanations are comparatively more supported. Even so, there is not complete explanations in the previous literature that may provide the comprehensive depiction of dividend policy. Since, no worldwide factors are suitable for the firms in different economies therefore dividend policy may become different pertaining to the numerous factors. However, the current study has highlighted one aspects of the several discussed in other studies and emphasizes on the need to address the board size with other key indicators by taking their interaction effect with board size in the dividend payout. Furthermore, the current study emphasizes on the need to conduct more studies on the board size and dividends by focusing on the characteristics of the board along with the along with the size of the board.

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