

## The Influence of Ownership Structure on Stock Repurchase Policy of Companies Listed in Indonesia Stock Exchange

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**Abstract:** *This study examines the influence of ownership structure on firms in Indonesia for their stock repurchase policy aimed to distribute excess funds to stockholders. Ownership structure studied consists of institutional ownership and managerial ownership. A sample of this study consists of 41 companies listed in the Indonesia Stock Exchange that repurchased their stocks from 2004 to 2013. The results showed that institutional investors and managerial ownership negatively affect the stock repurchase. Institutional ownership is considered able to be a useful monitoring tool to monitor the use of free cash flow in the company and mechanisms of control by the manager himself against the use of free cash flow is considered good. Moreover, they prefer to invest surplus funds in developing the company's business enterprises.*

**Keywords:** *Stock Repurchase, Ownership Structure, Institutional Investors, Managerial Ownership*

**Abstrak:** *Penelitian ini menguji pengaruh struktur kepemilikan pada perusahaan di Indonesia atas kebijakan pembelian kembali saham mereka yang bertujuan untuk mendistribusikan kelebihan dana kepada pemegang saham. Struktur kepemilikan yang dipelajari terdiri dari kepemilikan institusional dan kepemilikan manajerial. Sampel dari penelitian ini terdiri dari 41 perusahaan yang terdaftar di Bursa Efek Indonesia yang membeli kembali saham mereka selama periode 2004-2013. Hasil penelitian menunjukkan bahwa investor institusional dan kepemilikan manajerial berpengaruh negatif terhadap pembelian kembali saham. Kepemilikan institusional dianggap mampu menjadi alat pemantauan yang baik untuk memantau penggunaan arus kas bebas di perusahaan dan mekanisme kontrol oleh manajer sendiri terhadap penggunaan arus kas bebas dianggap baik. Selain itu, mereka lebih suka menginvestasikan dana surplus untuk mengembangkan perusahaan bisnis perusahaan.*

**Kata kunci:** *Pembelian Kembali Saham, Struktur Kepemilikan, Investor Institusional, Kepemilikan Manajerial*

## 1. Introduction

The stock repurchases one of the corporate actions in which the company buy back their shares from the market. Stock repurchase has increasingly become more popular, recently, in many countries, such as in the United States of America (USA), which contribute 44.42 percent of the total payout in 2000, compared to 11.82 percent of total payout in 1971 (Dittmar and Dittmar, 2002). In Indonesia, the regulation with regards to stock repurchase was introduced in 1998 in response to the increase of the stock repurchase transactions and of the needs of good corporate governance to protect minority shareholders' interest. The stock repurchase transaction in Indonesia is regulated through the issuance of Keputusan Ketua Bapepam Nomor: Kep-45/PM/1998 on August 14, 1998, with regards to the repurchase of shares issued by the public company. It was later changed into Bapepam Rule No. XI.B.2 to protect the rights of shareholders, especially minority shareholders because repurchase of this share is closely related to the agency conflict.

According to the signaling hypothesis, stock repurchase indicates that the company's stock price is undervalued (Vermaelen, 1981). Companies repurchase their shares after a decline in its price, and the price becomes less fluctuate after the repurchase (Ginglinger and Hamon, 2006). Hence, the stock repurchase could be one of the strategies to maintain stock liquidity or even increase it. Stock repurchase announcement might also imply that the company has produced excess free cash flow or company has managed to create decent profitability. In this case, the stock price would be expected to rise, and this would also imply an increase in shareholder wealth.

Furthermore, stock repurchase could also be used by shareholders as a control mechanism of the managers' performance. ElHoucine (2013) stated that any form of cash flow distribution (payout) to the shareholders is an efficient mechanism to mitigate agency conflict within a company. Dividends and stock repurchase are included as the cash flow distribution methods to the shareholders which are used as an instrument for the company to provide information (signal) to shareholders. El

Houcine (2013) argues that shareholders will consider dividend and stock repurchase as a signal of the company's business condition and prospects.

According to the free cash flow theory, the market reaction on the announcement day of stock repurchase reflects the availability of excess cash flow, or also known as, free cash flow that is still available after all of the company projects with positive NPV<sup>1</sup> have been financed. Jensen (1986) argued that such free cash flow would result in a conflict of interest between management and shareholders. The shareholders would prefer that all of the company's free cash flow to be distributed as dividends or stock repurchases, in the other hand, management would prefer to see the free cash flow to be used to increase company's revenue. However, should management choose to use the free cash flow to increase revenue, they might end up finance a project with negative NPV. Shareholders avoid this condition due to its higher risk characteristics. If the free cash flow distribution policy is intended to mitigate the agency conflict, the policy is likely influenced by the ownership structure (the ownership concentration and the nature of the shareholder) which is the critical element of the agency conflict.

Previous studies with regards to the ownership structure effect on stock repurchases policy show that institutional investors positively associated with the stock repurchase as the institutional investor may control managers by making them repurchase the company's floating shares to pay (distribute) the excess cash flow of the company to institutional investors. In this case, the stock repurchases are intended so that the excess cash flow is not used by the manager to finance projects with negative NPV (El Houcine, 2013).

The previous study also shows that managers use the stock repurchase as an entrenchment tool. Managers who are willing to increase their ownership in the company would consider committing on stock repurchase. By doing the stock repurchase, the ownership of external parties (outsiders) will be reduced, and the manager might buy the company's shares with a relatively discounted price, as the

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<sup>1</sup>NPV (*Net Present Value*) is the flow of future cost and benefit which is converted into the equivalent value today. A biggest positive NPV is the first reference in selecting investment in a project because NPV represents value for money/benefits that will happen in the future from an investment, in recent days (Ross, S.A., R.W. Westerfield, & B.D. Jordan, 2013).

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stock repurchase is likely to be done when company's shares are undervalued. Hence, the managerial ownership will increase, and managers' entrenchment level will be higher. Thus, in another word, managerial ownership affects the stock repurchase decision.

To date, only limited studies provide an empirical analysis of the effect of ownership structure on the stock repurchase in Indonesia. To the authors' best knowledge, no studies have been found to answer whether ownership by certain groups may affect the company's stock repurchase policy which is aimed to distribute the excess funds so that the funds are not being misused by the manager (agent). One thing that needs to be highlighted is whether the stock repurchase might be able to control managers in a way that stock repurchase would reduce the agency conflict in the case of Indonesia companies. This study will seek to answer that question, particularly the influence of ownership by institutional and managerial investors.

This study will replicate the approach conducted in a study by El Houcine (2013), which explored the effect of ownership structure by institutional and managerial on stock repurchase policy in France companies. El Houcine (2013) used a sample of the five years CAC 40 index which contains 40 France companies. This study, on the other hand, a used sample from Indonesia Stock Exchange (IDX), unlike El Houcine (2013), the research period is extended to ten years to capture the effect of ownership structure on stock repurchase policy in the Indonesian stock market.

## **2. Theoretical Framework and Hypothesis Development**

The ownership structure is a composition of a group of parties who own and control the company which consists of insider and investors ownership (Jahera and Lloyd, 1996). Company ownership indicates the voting rights on the company's economic decisions or also shows the control rights of the company's operations. In general, the shareholder structures that might influence management decisions are institutional investor and managerial ownership. The ownership structures, both managerial and institutional ownership, have different motivations in monitoring the company and management.

The corporate theory explains the reasons why the ownership structure and payout policy are associated. First, the agency theory states that with lower monitoring costs, managers have the opportunity to distribute more profit to investors. Jensen (1986) argued that extending monitoring, and companies are more likely to pay their free cash flow to investors. The ownership by larger institutional investors will result in a more massive payout (*ceteris paribus*). As previously discussed, the institutional investors would have more control over managers than other dispersed shareholders because they have a privileged position to access company's information and its competitors so that monitoring cost by institutional investors is lower.

Second, the adverse selection problem might result in investors with no information about the company to prefer dividends than stock repurchase (Barclay and Smith, 1988). On the other hand, the majority of shareholders, who have more information, do not face this problem. They prefer stock repurchase as it could increase the company's stock price. Therefore, when the institutional investors can get more information, they prefer companies who make payments in the form of stock repurchases than in the form of dividends.

Nowadays, the stock repurchase has become the alternative way to distribute funds to shareholders besides cash dividend. Fama and French (2001) recorded a significant decrease in the percentage amount of companies that distribute dividends, meanwhile, based on their observation since 1998, Grullon and Michaely (2002) found that the amount of the stock repurchase program is higher compared to the dividend. That was mainly due to the difference of the fiscal conditions between the two distribution types.

Tax treatments and rates of dividends are different compared to tax treatments and rates of capital gains obtained from the transaction of stock repurchase by the company. From tax management point of view, investors would prefer capital gain as it delays the actual tax payment until the profits are realized. On the other hand, the tax of the dividend payment must be paid at the time investors receive the dividend. Also, the tax rate of capital gains is smaller compared to the dividend tax rate (Jagannathan, Stephens and Weisbach, 2000). Likewise, in Indonesia, the tax rate of

capital gains amounted to 0.1% (Income Tax Laws article 4 paragraph (2c)), while the dividend tax rate is 15% for the corporate (Income Tax Laws article 23 paragraph (1a)) and 10% for individuals (Income Tax Laws article 17 paragraph (2c)).

Furthermore, the stock repurchase is considered as a positive signal for investors since in general company repurchasing their stock should they see the stock is undervalued, meaning that the intrinsic value of the company's stock is higher than its market price. The repurchase will reduce the number of outstanding shares in the market. After the stock repurchase, there is a possibility of an increase in stock price. Institutional investors as outsiders would expect such an increase in stock price.

A study conducted by Grinstein and Michaely (2005) provides some evidence with regards to the correlation between institutional ownership and payout policy due to oversight, as well as its implications to several payout theories that previously explained. First, when comparing the dividends paying and non-dividend paying companies, it is known that institutional investors would prefer the dividend-paying companies.

Second, institutional investors do not have any interest in the company that pays a high dividend. Conversely, institutional investors are believed would prefer the low-dividend stocks over the high-dividend stocks. Thus, there is no evidence to support the idea that higher dividends result in larger institutional investors ownership as implied in the previous theory. Interestingly, these results are consistent with management's perception of the impact of payout policy to investors in which manager believes that, compared to institutional investors, individual investors are more interested in the increase of dividend (Brav et al., 2005).

Third, Grinstein and Michaely (2005) also found that institutional investors would prefer to invest in companies that repurchase their stock. Companies that repurchase their stock have relatively greater institutional ownership than companies that do not repurchase their stock. Hence, it could be said that institutional ownership positively associated with the company's stock repurchase policy. Fourth, institutional ownership and concentration of ownership do not make the company increasing the payout. Thus, the positive association of institutional ownership with the stock repurchase is

consistent with agency theory proposed by Jensen (1986) and adverse selection theory proposed by Barclay and Smith (1988).

Also, the positive association of institutional ownership with the stock repurchase is also supported by the difference in fiscal condition characteristics between the types of shareholders which result in investors to have different views regarding the free cash flow distribution. In UK taxation system, institutional investors will be subject to tax on dividend whereas the tax on the dividend is not applied for individual investors. This difference in taxation treatment affects the view of each investor on the free cash flow distribution policy of the company (Rau and Vermaelen, 2002). Such conditions may also apply in Indonesia considering the dividends paid to institutional investors will be subject to 15 per cent of the gross amount as specified in the Income Tax Law article 23 paragraph (1a), while dividend payments to individual investors will be subject to a lower tax rate of 10 percent at the highest as stated in the Income Tax Law article 17 paragraph (2c). Thus, the institutional investors who apply tax management would be more interested if the company distribute the free cash flow to them through stock repurchases.

Meanwhile, according to financial theory, the institutional investor ownership is negatively associated with the repurchase policy since they prefer the funds to be reinvested in projects. Payment rates decrease when the majority shareholder is a company or a financial institution that has an affiliation with a group of companies (Maury and Pajuste, 2002). Hence, possibility for such companies can choose to hold the funds and engage in group projects. From the explanations above, the following hypothesis can be concluded:

**H1.** *There is an influence of the institutional investor's ownership (outsiders) on the company stock repurchase policy.*

The company will be jeopardized if the managers act on their own interests and not for the benefit of shareholders. Such a condition leads to the agency conflict between the manager and shareholders of the company (Godfrey et al., 2010). Each party has a different purpose and risk preference which are related to their behavior. If

the manager fails to perform well, their positions would be at risk as they could be no longer assigned as the manager of the company, on the other hand, shareholders' stakes would be at risk should they chose the wrong managers. This is the consequence of the separation between ownership and management functions. Agency conflicts can be minimized if the manager is also the owner of the company or vice versa. In that condition, the manager will align his own interests with the interests of shareholders.

According to the alignment of interest theory, the more shares owned by managers, the objectives of managers and shareholders will be more aligned (Charlier and Du Boys, 2010). Managers will be more motivated to seek profitable projects, and their interests will be more aligned with the interests of other shareholders as the shares held by the manager's increase. This implies a cost reduction in conducting control of the manager. By doing so, the monitoring mechanism using the payment of dividends or stock repurchase is not so necessary. Charlier and Du Boys (2010) found that the distribution of free cash flow is negatively associated with the interests of managerial shareholders, this is due to the interests of agent and principal are aligned.

However, based on the theory of entrenching the managers, Harvey, Collins, and Wansley (2003) state that at a certain level of ownership, managers would take advantage of the control power they have which strengthen their position and not maximizing the company's value. This is indeed not in line with the interests of shareholders who want to maximize the company's value. This difference in managers' and shareholders' interest will result in the agency problem. Thus, the company needs a supervisory mechanism to mitigate the harmful impact of this agency problem. One of the supervisions that can be done by shareholders is through the company's payout policy. One of the methods of payout policy is the stock repurchase program by the company, and this method is aimed so that managers not to invest in projects with negative NPV. Therefore, from the discussion above, the following hypothesis can be concluded:

**H2.** *There is an influence of managerial ownership (insiders) on stock repurchase policy of the company.*



### 3. Research Methods

This study was conducted to analyze the effect of ownership, which includes institutional and managerial ownership, on the company's decision to repurchase its shares in the market. The population of this study is all companies listed on the Indonesian Stock Exchange (IDX). The data used for this study is based on the company that repurchases its shares from the market so that the sample used in this study are companies listed on the IDX that repurchase shares over 2004 to 2013 (share repurchase data is obtained from the Bapepam-LK Annual Report). This observation period was selected in this study after considering the availability of data.

To examine the influence of institutional and managerial ownership on the stock repurchase transaction, a sample of financial companies are not included in this study, and this is because the corporate governance systems, financing regulation, as well as stock repurchase regulation of financial companies are different compared to companies in other industries. This study also excludes State-Owned Enterprises (SOEs) as the government ownership will be higher than the institutional investor ownership and managerial ownership.

Furthermore, to obtain the shares repurchase data resulting only from the company's payout decision, the authors eliminate all of the shares repurchases which are aimed to exercise convertible bonds, employee stock option plans (ESOP), control stock price to gain profit, go private (delisting after repurchasing the stocks), or conduct investments (such as merger). Based on those pre-determined criteria, 59 share repurchases of companies from various industry listed on the Stock Exchange are used in this study.

The regression model in this study is closely related to the El Houcine (2013) study, with some modifications. The following regression model used in this study:

$$\text{Net Repurchase} = \beta_0 + \beta_1 \text{INS} + \beta_2 \text{MNG} + \beta_3 \text{SIZE} + \beta_4 \text{DEBT} + \beta_5 \text{FCF} + \beta_6 \text{ROA} + \beta_7 \text{DIV} \quad (3.1)$$

Information:

*Net Repurchase* = the stocks repurchase by the company

*INS* = institutional investor ownership

*MNG* = managerial ownership

*SIZE* = company size

*DEBT* = debt to assets ratio of the company

*FCF* = free cash flow

*ROA* = return on assets

*DIV* = dividend distribution rate

The dependent variable in this study is the net repurchase and the independent variables consist of holdings by institutional investors (*INS*), managerial ownership (*MNG*), company size (*SIZE*), debt to assets ratio of the company (*DEBT*), free cash flow (*FCF*), return on assets (*ROA*) and the level of dividend payments (*DIV*). Definitions and descriptions of each variable as follows:

*a. Net Repurchase*

Net Repurchase is a dependent variable which, in this study, is influenced by the nature of the institutional investor's ownership, company insiders, and several other independent variables such as company size, debt to total assets ratio, free cash flow, return on assets and dividend payments level. The available data may include several forms of repurchase by the company, such as stock repurchase, transfers (conversion of bonds into shares) and the cancellation which is related to the company's objective on the purchases. To separate the repurchase of shares resulting from the payout decision, the authors exclude all accomplished repurchases intended for employee stock option plans (*ESOP*), controlling the price (controlling stock prices to gain profit, usually treasury stock from stock repurchase is sold back in a short period after the stock repurchase date) or an investment (such as merger). Thus, Net Repurchase will be obtained. Net Repurchase is measured using the number of stocks repurchased by the company for one year, then is deducted by the shares sold and transferred.

*b. Institutional investors ownership*

The institutional investor's ownership (INS) is a percentage of the company's shares held by institutional investors which are measured by the number of shares held by institutional investors divided by the total number of outstanding shares on December 31. The number of shares held by institutional investors is obtained from the companies' financial statements and annual reports.

$$INS = \frac{\text{Number of shares held by an institutional investors}}{\text{Total number of outstanding shares}} \quad (3)$$

Allen et al. (2000) show that institutional shareholders are more capable of controlling managers than another type of shareholders. They have a privilege to access corporate data so that they would have more influence on the company's financial decisions, particularly the decision of payout policy in the form of stock repurchases.

*c. Managerial ownership*

Managerial ownership (MNG) is the percentage of shares held by managers, employees, directors and/or commissioners in a company (insiders). The number of shares held by them is identified from the company's financial statements.

$$MNG = \frac{\text{Number of shares held by employees, directors and commissioners}}{\text{total numbers of outstanding shares}}$$

(3.3)

According to the theory of interest convergence (Jensen and Meckling, 1976), the ownership of the company's capital by the manager is a good incentive for them to run the company in line with shareholder interests. As the managerial ownership increase, the level of divergence (dispersion) between shareholders' and managers' decrease. Therefore, the function of the stock repurchase policy as a control mechanism becomes useless.

*d. Companies size*

In this study, the size of the company is calculated based on the total assets shown in its financial statements. Measurement of the company size is proxied by the logarithm of the total assets of the company. The use of logarithms is aimed to smooth the magnitude of the numbers and proportionate the company size variable with other variables of the current regression. Company size is denoted by SIZE.

$$\text{Company Size} = \text{Log}(\text{Total Aset}) \quad (3)$$

*e. The debt to assets ratio of the company*

This variable reflects the ratio between total debt (current liabilities and long-term debt) and the sum of all assets listed in the company's financial statements. This ratio shows the proportion of the total assets financed by debt. This variable is denoted by DEBT.

$$\text{DEBT} = \frac{\text{Total Debts}}{\text{Total Assets}} \quad (3.5)$$

*f. Free cash flow*

This variable reflects cash available or held by managers to meet the needs of the company after deducting for financing expenditures and maintenance capital expenditures (discretionary funds). Free Cash Flow calculation is based on net income deducted by dividends, added by depreciation and then divided by the total assets of the company. FCF denotes free cash flow.

$$\text{FCF} = \frac{\text{Net Profit} - \text{Dividends} + \text{Depreciations}}{\text{Total Assets}} \quad (3)$$

*g. Return on Assets*

ROA is a proxy for profitability that reflects the company's ability to generate profits. ROA calculation is based on net income divided by total assets of the company.

$$ROA = \frac{Net\ Profit}{Total\ Assets} \quad (3.7)$$

#### *h. Dividend Payout level (DIV)*

This variable reflects the level of dividend distribution to the shareholders which is proxied by the value of the natural logarithm of the dividends to net income ratio. DIV denotes dividend distribution rate.

$$DIV = Ln\left(\frac{Dividend}{Net\ Profit}\right) \quad (3.8)$$

Data processing is designed to statistically examine the causal correlation between the independent variables and the dependent variable using pooled data. The collected data is the sample obtained from the population, so it might deviate from the population which the value is unknown. The accuracy of the sample observation value is determined by error. Therefore, this study used the least squares method, or commonly known as OLS (Ordinary Least Square). OLS is a method used to achieve the minimum deviation or error by looking for estimator (regression coefficient) which produce the smallest error. To achieve the regression model might best represent the population, the regression coefficients must be BLUE (Best Linear Unbiased Estimate) which has the characteristics of linear, unbiased and has minimum variance.

## **4. Result**

### *4.1 Descriptive Statistics*

Table 1 shows the statistic description of all variables used in the research model. The mean of Repurchase Net is 98,173,667 shares. That amount is greater than the average amount on a similar study conducted by El Houcine (2013) in companies in France amounted to 1,494,767 shares. Based on this numbers, it can be said that companies in Indonesia tend to repurchase shares in a more significant amount. This variable's standard deviation value is

110.000.000. This value indicates that data deviation is 110.000.000 of the arithmetic mean.

Table 1  
Descriptive Statistics

	Mean	Standard-deviation	Minimum	Maximum	Median
<b>Net Repurchase</b>	98.173.667	110.000.000	359.500	335.699.000	51.062.000
<b>INS</b>	0,6151	0,2238	0	0,9977	0,6429
<b>MNG</b>	0,0395	0,1476	0	0,7916	0
<b>SIZE</b>	9,3626	0,6286	7,9514	10,4191	9,3281
<b>DEBT</b>	0,1882	0,1632	0	0,5782	0,1632
<b>FCF</b>	0,0781	0,0574	-0,0899	0,2831	0,0681
<b>ROA</b>	0,0684	0,0765	-0,0913	0,4527	0,0456
<b>DIV</b>	-1,0414	1,1723	-6,0128	0,9221	-0,9142

The mean of INS is 61.51%, it has minimum and the maximum value of 0% and 99.77% respectively. Given the average value, it can be implied that the percentage of ownership held by institutional investors is the highest (61.51%) among the other ownership type. This result indicates that companies in Indonesia tend to have more shares held by institutional investors rather than by managerial. The standard deviation value which is 0.2238 shows that data deviation is 0.2238 from the arithmetic mean.

The mean MNG is 3.95%, it has a minimum and the maximum value of 0% and 79.16% respectively. This average value is lower than institutional ownership's average value. The median of MNG is zero which indicates that companies' ownership by managers tends to be minimum in Indonesia. The standard deviation value is 0.1476 which suggests the data deviation is 0.1476 from the arithmetic mean.

The mean SIZE is 9.3626, and it has minimum and the maximum value of 7.9514 and 10.4191 respectively. This value indicates that the majority of companies in the sample is large. It can be inferred from the average value of 9.3626 which is approaching its maximum value rather than its the minimum value.

Table 1 shows that the average, maximum and median value of DEBT (debt ratio) is quite small. This illustrates that companies in the sample more prefer to fund their investment equity issuance and tend to avoid the risk of using high levels debt.

The mean of FCF is 0.0781 with a standard deviation of 0.0574. The value shows that data deviation at 0.0574 from the arithmetic means. The mean value indicates that most of the companies in the sample have a relatively same free cash flow of around 7.81% of total assets. It was also shown by the standard deviation which is not too large.

In Table 1, the mean of ROA is 0.0684, and it has minimum and maximum values of -0.0913 and 0.4527 respectively. Provided the mean, minimum, maximum and standard deviation, as well as the similar companies which have minimum and maximum value shows, it can be seen that there is similarity of FCF variable pattern. This illustrates that the companies in the sample have increased their free cash flow along with the increased performance of the company. Furthermore, the mean value of DIV is -1.0414, it has minimum and maximum values of -6.0128 and 0.9221 respectively. The standard deviation value is 1.1723 which implies that the data deviation is at 1.1723 from the arithmetic mean.

#### 4.2 Regression Test

After some tests have been conducted to obtain a robust research model, the estimated coefficients are believed to have the properties of BLUE. Table 4.2 presents the final results of the estimates used for the analysis in the statistical test:

From Table 2, it can be seen that the adjusted  $R^2$  value is 0.2812 which indicates that independent variables explain 28, 12% of the variance of the dependent variable. In other words, 71.88% of the dependent variable's variance can be explained by other factors outside the model.

The results show that institutional ownership is negatively associated with stock repurchase policy as reflected in the value of the regression coefficient. The negative effect of institutional ownership on the stock repurchase can be explained by the fact that institutional investors can control managers better than another type of

shareholders. This is because they have the privilege to access company’s and its competitors’ information so that the monitoring cost by institutional investors is lower than other shareholders (Shleifer and Vishny, 1986 as well as Allen et al., 2000). Also, institutional ownership in Indonesia can become an effective supervision mechanism. This is because institutional shareholders have the capability and resource to oversee the companies they invest in (Swandari, 2003). Thus, it can be concluded that the stock repurchase policy as a supervisory mechanism does not function well since the by the institutional investor's capability can mitigate the agency conflict and resource. Hence, they are unlikely to increase the number of shares acquired. Besides, the stock repurchase could reduce their ownership portion that would also reduce their control rights.

Table 2  
The result of Estimated Regression Equation

Estimated Regression Equation		
Variables	Coefficient	Prob (t-Statistics)
INS	-208.000.000***	0,0028
MNG	-204.000.000*	0,0683
SIZE	59.413.619**	0,0189
DEBT	-10.482.630	0,9106
FCF	919.000.000*	0,0680
ROA	-764.000.000**	0,0409
DIV	3.733.464	0,7683
<b>Prob (F-Statistical)</b>		0,000936
<b>Adjusted R-squared</b>		0,28118
<b>Observation Amount</b>		59

\*\*\* = significant at  $\alpha = 1\%$ .  
 \*\* = significant at  $\alpha = 5\%$ .  
 \* = significant at  $\alpha = 10\%$ .



Managerial ownership is negatively associated with the stock repurchase policy. The influence of managerial ownership on stock repurchase can be explained by the alignment of interest theory which states that the more shares held by managers, the more managers' and shareholders' objectives are aligned. Managers would be more motivated to seek profitable projects rather than using the excess funds to repurchase the company's shares. They also would be more careful in deciding since the manager could feel the direct benefits or loss resulting from their decisions. Also, because of the less agency conflict, the monitoring mechanism using the free cash flow distribution is not so necessary (Charlier and Du Boys, 2010). Thus, it can be concluded that the stock repurchase policy as a monitoring tool is not effective since agency conflict is already mitigated by the aligned objectives between managers and outsiders shareholders so that they tend to reduce the number of shares acquired. Also, managers will be more interested in investing in projects to increase revenue.

Furthermore, the SIZE variable (company size) as measured by total assets indicate a positive association on the stock repurchase. These results suggest that small companies are more motivated to invest 100% of their cash flow to accelerate the company's growth. Meanwhile, large companies are more likely to generate cash flow more than they need to finance all attractive investment opportunities compared to small companies (Berk and DeMarzo, 2013). When a company has excess funds, they might distribute it (payout) to shareholders. Therefore, large companies are more capable of doing stock repurchase than smaller companies. This illustrates that the size of the company affects the stock repurchase policy on companies listed in IDX.

From Table 2, it can be seen that the variable DEBT has no significant effect on the Net Repurchase. Thus, the strong relationship of financial leverage and stock repurchase cannot be found in companies listed in the IDX. This indicates that the leverage ratio is less likely associated with companies' stock repurchase policy. Thus, it can be concluded that only a few of companies listed on the Stock Exchange conduct the stock repurchase to achieve targeted capital structure.

In this study, free cash flow has a positive association with the stock repurchase. For companies listed in the Stock Exchange, the availability of free cash flow

motivates the company to repurchase their shares to reduce the agency conflict. Such free cash flow is derived from the unstable increasing profit. If the free cash flow is derived from a stable profit, in the long run, the company would be more likely to increase the dividend payout (Jagannathan, Stephens and Weisbach, 2000).

In this study, ROA (profitability) has a negative effect on the stock repurchase. Given this result, the effect of ROA on Repurchase Net can be explained by previous studies that show that companies prefer to pay more dividends as it can be seen as a good signal of stable profitability in the long run. Higher profitability ratio indicates that the company can generate a stable profit in the long run because the profit is generated from the company's asset management (Jagannathan, Stephens and Weisbach, 2000). It illustrates that the company's performance is a factor which is considered by companies on the Stock Exchange in the stock repurchase decisions.

Table 4.2 shows that the strong association of the dividend payout level with stock repurchase cannot be found in companies listed on IDX. This illustrates that the dividend payout level is not a substantial factor that influences stock repurchase. Thus, it can be concluded that companies listed on IDX are not likely to take the dividend payout level consideration into account when they decide to repurchase their shares.

## **5. Conclusion**

Based on the results, it can be inferred that institutional ownership is negatively associated with the stock repurchase policy of companies listed on IDX. This result is consistent with the previous studies conducted by Maury and Pajuste (2002) who found similar results. Furthermore, this study also found a negative association of the managerial ownership policies with the stock repurchase in companies listed on IDX. This result can be explained by the alignment of interest theory(Charlier and Du Boys, 2010).

Furthermore, the results of this study illustrate that companies in Indonesia specifically those who listed on IDX are likely to have relatively smaller managerial ownership than institutional ownership. However, the result, which is associated with the alignment of interest theory, implies that the control mechanism by the manager

himself on the use of free cash flow is sufficient. Also, institutional ownership is considered as an effective monitoring tool to monitor the use of free cash flow in the company. Hence, stock repurchase as a control mechanism does not work in Indonesia. Meanwhile, managers use free cash flow in the company to be reinvested more carefully to increase the performance of the company.

Stock repurchases by companies in Indonesia most likely are aimed to increase the shareholder value, restore investor trust due to a financial crunch in 2008, maintain the stability of earnings per share due to the fluctuation of macroeconomic conditions and partly intended to ESOP (Employee Stock Option Plan).

There are several limitations to this study. This study does not consider the macroeconomic conditions, such as the economic crisis and significant fluctuations of the Jakarta Composite Index that may affect the stock repurchase policy. Also, the sample size of this study is limited since there are only a few companies who conducted the stock repurchase. Further research may consider increasing the number of samples and the observation period to obtain a more in-depth result.

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