Board Governance, Dividend Payout and Executive Compensation in Malaysian Firms

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Abstract: Research Question: This study seeks to present and test how board governance mechanisms affect the relationship between a company's dividend payout and CEO compensation. **Motivation:** In the face of the significant payouts to directors and abundant literature on executive pay, there is scant evidence on board governance the relationship between executive compensation and the dividend payout policy of listed firms in emerging capital markets. The independent variable used in this study is the dividend payout ratio, which is the dividend per share divided by primary earnings per share before extraordinary items. A direct measure of the dependent variable is the total executive compensation, inclusive of fixed salaries and variable bonuses. The research is built based on these three key papers, Bhattacharyya *et al.* (2011); Smith and Watts (1992); Gaver and Gaver (1993). **Idea:** Building on Bhattacharyya *et al.* (2011), this study examines how the board governance relationship between a company's dividend payout and executive compensation in the context of a developing country. **Data:** Using a sample of 300 largest Malaysian public listed companies (PLCs) on Bursa Malaysia from 2008 until 2014. The data is from the Kuala Lumpur Stock Exchange, OSIRIS, DATASTREAM, BANKSCOPE databases, and the Malaysian Stock Performance Guide. **Method/Tools:** We test using the panel data. **Findings:** Our empirical results reveal three findings. First, our results suggest a direct relationship between dividend payout and executive compensation across all models. Our sub-sample analyses show that this phenomenon is limited to the non-government linked firms and non-family firms. Secondly, board governance shows that the Bumiputera, CEO-education, and non-executive directors are positively related to dividend payout. Lastly, the interaction between executive board compensation and the presence of Bumiputera has a negative relationship with the dividend payout. **Contributions:** The results of this study contribute to the growing scholarly work that examines board governance and the impact on dividend payout in an emerging market context.

Keywords: Executive compensation, board governance, dividend payout, Malaysia.
JEL Classification: G35, J33, N25

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1. Introduction

Higher directors' remuneration does not necessarily equate to better financial performance for many public listed companies (PLCs) in Malaysia. Despite falling revenues and profits, approximately 50 loss-making companies offered handsome windfalls to their directors. The Malaysia Asian Corporate Governance Report 2015 found that 850 PLC's executive directors' remuneration on average grew by 14.2 percent (2014: RM1.34 mil to 2015: RM1.53 mil) while non-executive 'directors' fee surged to 19.4 percent (2014: RM98,000 to 2015: RM117,000). In his annual letter to shareholders, Warren Buffet reported that U.S. companies' director's compensation has now soared to a level that inevitably makes pay a subconscious factor affecting the behaviour of many non-wealthy members.' "Think, for a moment, of the director earning $250,000-300,000 for board meetings consuming a pleasant couple of days six or so times a 'year.'

As per Corporate Blueprint, the Malaysian Code on Corporate Governance (MCCG) introduced in 2011 transformed excellence in corporate governance and subsequently reviewed in 2012, 2017, and 2020 to promote greater internalization of corporate governance culture. It is one of the Malaysian government's priorities to increase the competitiveness of Malaysian businesses and attract foreign investments. In the MCCG 2020 report, the Securities Commission (SC) focused on ensuring the remuneration commensurate with individual and company performance; many of these companies have formalized a remuneration policy to guide the determination of incentive structures and remuneration. These developments portend well for our study's timing that focuses on corporate governance, executive compensation, and dividend payout to strengthen the management policies of PLCs. In the face of the significant payouts to directors and abundant literature on executive pay, there is scant evidence on the relationship between executive compensation and the dividend payout policy of listed firms in emerging capital markets.

Shareholders have little public success in forcing company boards to justify the 'executives' pay arrangements, and often their complaints about excessive handouts have fallen on deaf ears. Furthermore, another contentious issue reported by Wall Street Journal, dated April 29, 2021, found that ' 'CEO's remuneration skyrocketed in 2020. The Wall Street Journal analysed the remuneration for more than 300 S&P 500 'CEOs who had been in their roles for at least a year and found that their median pay increased from $12.8 million in 2019 to $13.7 million in 2020. Reddy *et al.* (2015), who did a similar study, found that remuneration for performance is weaker at a higher level of managerial ownership. They envision that both the principle-agent and administrative power explain executive pay.

Interestingly, Malaysia's political system affects the severity of agency problems between the 'stakeholders' (Benjamin *et al.*, 2016). Other studies that opine the impact of whether a listed company is government-owned or politically connected CEOs are such as Kasipillai *et al.*, 2017; Minhat and Abdullah, 2014, and Tee *et al.*, 2017. Given concentrated managerial ownership and politically connected executive directors in Malaysian PLCs, the Board of directors is prone to compensate the insider owners, which may cause the pay for performance relationship to be weak, which influences dividend payouts.

Executive director's compensation is a controversial subject that has attracted legislators, the media, and academicians in the U.S., the U.K., and Portugal (Bebchuk and Fried, 2003; Conyon and Murphy, 2000). In the context of Portuguese firms, Alves *et al.* (2016) posited that specific factors such as shareholders return, firm characteristics, CEO characteristics, and the profile of Board of directors could account for the majority of the variance in total executive remuneration. In New Zealand, Reddy *et al.* (2015) found that after controlling for firm size, performance, Industry, and year effects, the CEO's compensation inclines towards interior corporate governance features rather than external corporate governance

practices. Studies also exhibited that companies having CEOs on boards have the power to influence remaining board decisions, which causes the boards to become less expedient in monitoring compensation (Lee and Isa, 2015; Benjamin and Zain, 2015). Conyon and He (2011) documented that in the U.S., 'executives' compensation is about seventeen times higher than in China. Besides the significant differences in the U.S., China executives' pay persists even after controlling economic and governance factors.

Bhattacharyya *et al.* (2011) advanced the agency paradigm theory to expound the dividend puzzle and found that payout ratios and managerial compensations are negatively related. Furthermore, they revealed a negative relationship between dividend payout ratio and executive compensation in the U.S. and Canada due to their similarity in their corporate governance structures and legal frameworks. Building on Bhattacharyya *et al.* (2011), studies examine how the board governance relationship between a company's dividend payout and executive compensation in the context of a developing country. The results of this study contribute to the growing scholarly work that examines board governance and the impact on dividend payout in an emerging market context.

The remainder of the paper is structured as follows: Section two reviews prior literature and develops testable hypotheses. Section 3 discusses the research design, including details of the sample, models, and methodology. Section 4 presents the empirical results, and Section 5 concludes the paper.

2. Literature Review and Hypotheses Development

Malaysia has a unique institutional setting. It is a multiracial developing country with different levels of investor protection, legal regime, corporate policies, and ownership structure; hence, evidence from Anglo-American jurisdictions may not generalize to Malaysia. The Securities Commission of Malaysia released the Corporate Governance Blueprint in 2011, 2012, 2017, and 2020. The MCCG 2012 focused on strengthening board structure and composition, recognizing the role of directors as active and responsible fiduciaries. Subsequently, there was a release of MCCG, 2017 and 2020 by Bursa Malaysia. One of the significant highlights of the blueprint was on the "Boards as active and responsible fiduciaries," The design establishes a mandatory formal board charter that enables industry-led studies on directors' compensation.

2.1 Dividend Payout and Executive Compensation

The question of why companies pay dividends has continued to puzzle researchers for an extensive review of the literature (see Obradovich and Gill, 2012). Harris (2008) and Perel (2003) posit that the business ethics literature raised concerns about unethical and unreasonable compensation policies that deprive shareholders of their fair share of a company's wealth. Smith and Watts (1992) argued that, after controlling for the effects of growth opportunities and firm size, lower dividend yields correspond with higher levels of executive compensation because of the link between a firm's financing and dividend policies. Gaver and Gaver (1993) also corroborated with the findings of Smith and Watt's (1992) study at the firm level.

On the other hand, Golec (1994) study provided evidence from a real estate industry perspective. In typical wage contracts, the total compensation is associated with higher dividend yields than a discretionary-based payment. Likewise, White (1996) found a direct association between the dividend and 'executives' incentives for the oil and gas, defence/aerospace, and the food processing industries. White (1996) showed that management compensation is positively associated with higher dividend payouts, yields, and more significant annual dividend levels. White's (1996) study evidenced an association between firm characteristics and the use of compensation contracts with a dividend

provision, which led him to conclude that his results are consistent with the theory that firms' link compensation incentives to dividend payouts reduce agency conflicts shareholders and management.

The study of 1,650 public listed firms in the UK, Germany, France, Italy, Netherlands, and Spain from 2002 to 2009 by De Cesari and Ozkan (2015) found that executive stock option holdings and stock option deltas have an adverse impact on the total dividend payout and hence, implying that 'executives' compensation is not a substitute for share repurchase or dividends. In Malaysia, share repurchases are not typical, enabling us to focus solely on the dividend payout as the primary means to reduce the vertical agency conflict between shareholders and management.

Anderson *et al.* (2020) analysed data for New Zealand firms' dividend payouts over 1997–2015 and found consistent results with Bhattacharyya *et al.* (2008). Their results indicated that corporate dividend policy among New Zealand firms is most appropriate by considering the dividend payout ratio rather than the level of, or changes in, cash dividends alone. Bhattacharyya *et al.*'s (2008) study are particularly relevant as it emphasizes the advanced theory of the agency paradigm. They found that dividend payout is negatively associated with executive compensation, and these results hold when a payout is in the form of ordinary dividends or common share repurchases. Bhattacharyya *et al.* (2008) has advanced a theory based on the agency paradigm that dividends resolve agency issues of managerial compensation contracts. Therefore, we state the following hypothesis:

H_1: *Ceteris paribus has a negative relationship between dividend payout and executive compensation.*

2.2 Board Governance
This section outlines various elements of board governance and its linkage with the dividend policy of firms.

2.2.1 Remuneration Committee
The prior studies reviewed the literature on internal governance mechanisms. For example, Smith Committee posited that the corporate governance factors and top management remuneration had gained much interest by researchers due to the growing concerns of the authorities regarding firms' internal monitoring. Vafeas (2003), who studied the director's committee in firms, found that directors with 20 or higher years of board service are almost twice as likely to be in an affiliated profession to managers versus other directors who are more likely to serve on a firm's nominating and compensation committees. Furthermore, Kanapathippillai *et al.* (2016) found that the remuneration committee's existence and quality play a significant role in providing voluntary disclosure of remuneration actions and influences the extent of the exposure. In addition, Kanapathippillai *et al.*'s (2016) study reported that remuneration committee independence and diligence enhance the quality of remuneration committees. Alves *et al.* (2016) found that board committees[1] and the presence of the remuneration committee were positively related to the executive earnings.

In contrast, Pahi and Yadav (2019) documented that executive compensation has a significant agency problem that arises from partial contracting. The management can expropriate shareholder wealth through higher salary packages and more perks. Pahi and Yadav's (2019) studies showed that the executive committee indicates a positive but insignificant relationship with dividend policy.

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[1] Such as remuneration committee, fiscal board, auditing committee, and others.

Based on the mixed evidence as to whether an independent remuneration committee helps monitor executive compensation and to link to a firm performance that in turn affects dividend payout, we state the following related hypotheses:

H₂: Ceteris paribus, there is a relationship between the remuneration committee and dividend payout.

2.2.2 CEO Education

Prior studies, such as Carpenter and Westphal (2001), argued that directors' educational background plays an essential role in facilitating the strategic decision-making process. Dragoni *et al.* (2011) posit that better-educated CEOs have more good training, substantial cognitive growth, a wealthy knowledge base, and possibly intensifying future firm performance by developing their decision-making and encouraging more relevant strategic actions. In contrast, Serra *et al.* (2016) argue that CEOs' competence indicated that there is no enhancement in performance in firms where the CEO possesses better educational qualifications.

Darmadi (2013) documented that other factor such as experience, managerial skills, networks, and skills obtained outside of formal school education also affects the relationship between directors and firm performance. In this sense, there is room for so-called "street smart" directors to play a vital role in the boardroom. These "street smart" directors may be less educated. Still, due to their long working association with the firms they work for, their knowledge of the firms' business's intricacies is also highly valued. As such, we cannot predict the direction of the relationship, so we posit the following non-directional relationship.

H₃: Ceteris paribus, there is a relationship between CEO education and dividend payout.

2.2.3 Board Independence

Each country's legal, political, and institutional environments significantly affect firms' corporate governance mechanisms favoured. The "Board composition," an integral part of the institutional environment, is ordinarily defined as the proportion of outside directors to total directors (Lee and Isa, 2015; Roy, 2015; Kesner, 1987). These researchers documented that the components of the Board are necessary to judge its monitoring effectiveness. In the Malaysian context, Abdullah (2006) reiterated that board composition is not random but based on other factors, including political considerations.

The additional factors that influence the decision of board composition in Malaysia are the size of the Board, the extent to which the directors are independent of the firm's management, the length of directors' shareholdings, CEO duality, and the presence of block shareholders. Rashidah and Roszaini (2005) argued that more independent directors' representation on the corporate Board did not limit a firm's earnings management practices. Sharma (2011) articulated that after controlling for the effects of CEO entrenchment and ownership determinants of the propensity to pay dividends, there is evidence of a positive relationship between the tendency to pay and the number of independent board members. Furthermore, numerous studies suggested the ideal board size to be in the range of seven to eight (Lee and Isa, 2015; Roy, 2015; Kesner, 1987; Rashidah and Roszaini, 2005; Abdullah, 2006). Several other studies document mixed results on the effectiveness of board size and 'firms' earnings (Lee and Isa, 2015; Roy, 2015). Therefore, we state the following hypothesis:

H_4: Ceteris paribus, there is a relationship between board independence and dividend payout.

2.2.4 Bumiputera on the Board

In Canada, Latin America, the U.K., and the U.S., ethnically diverse companies are 35 percent more likely to outperform their peers. However, unlike in developed countries, where the demand and supply for skills drive board diversity, this is not the case in Malaysia. In Malaysia, board diversity is primarily driven by the affirmative New Economic Policy (NEP) programs that require firms listed in Bursa Malaysia to reserve a minimum of 30% board seats or equity to the ethnic Malays[2] (Gomez *et al*., 1999). Subramaniam *et al.* (2020) revealed that the positive relationship between executive compensation and dividend payout is more evident in politically connected firms.

The NEP, established in 1970, was used to reduce equity ownership imbalance between the various ethnic groups by increasing Bumiputera's equity ownership of firms listed in the capital market (Tan, 2004). Haniffa and Hudaib (2006) and Yatim *et al*. (2006) argued that ethnicity in Malaysia has, to a considerable extent, shaped how the country and businesses are managed due to external political intervention and internally via its Islamic cultural values. However, it is unclear whether board ethnicity affects dividend decisions and, thus, is concurrently associated with executive compensation.

Bolbol (2012), in a Malaysian study, found that the ethnicity of the Board of directors is correlated negatively and insignificantly to dividend payout. In contrast, the study by Iskandar *et al.* (2017) suggested that Bumiputera's on boards can positively impact dividend payout. Subramaniam *et al*. (2014) found that firms' growth opportunities are associated with fewer dividends payouts and that this relationship is weaker for Bumiputera ethnic-controlled firms. The result to date supports the fact that the negative association exists only for non-GLCs. Based on the overall findings, and due to the mixed results, we state the hypothesis as below:

H_{5a}: Ceteris paribus, there is a relationship between Bumiputera directors on the board and dividend payout.

In addition to the above hypothesis, we moderate the executive compensation with the Bumiputera directors on the Board to see the impact on dividend payout. We state the interaction hypothesis as below:

H_{5b}: The relationship between dividend payout and executive compensation is minimalized by the effect of Bumiputera directors on the Board.

3. Research Design and Methodology
3.1 Sample Selection

The sample consists of 300 of the largest companies listed on Bursa Malaysia for the seven years 2008 to 2014, surrounding MCCG reforms and their implementation during the 2012-2013 periods. The data is from the Kuala Lumpur Stock Exchange, OSIRIS, DATASTREAM, BANKSCOPE databases, and the Malaysian Stock Performance Guide. In addition, we obtained the ownership data and control variables from the OSIRIS and Bloomberg databases and company annual reports available on the Bursa Malaysia website. The variable labels, definitions, and measurements are presented in Appendix A. After eliminating the missing data, the sample size is reduced to 287 firms (See Table 1).

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[2] Referred to as natives or Bumiputera.

The industry distribution depicts that most observations are from the properties/hotel sector (29.27 percent), closely followed by the trading and services sector (23.69 percent) and industrial product sector (22.66 percent), respectively, from the sample size. The statistical package STATA is used to conduct the data analysis.

Table 1: Sample selection criteria

Classification	No of companies	Firm year observations	Percentage (%)
Consumer product	32	224	11.14
Trading/services	68	476	23.69
Properties/hotel	84	588	29.27
Construction	11	77	3.83
Plantations	27	189	9.41
Industrial products	65	455	22.66
Total companies and firm year observations	287	2009	100

3.2 Dependent Variable

Gaver and Gaver (1993) used the dividend payout ratio and the dividend yield as two dividend policy measures. The dividend payout ratio (DIV_POUT) is the dividend per share divided by primary earnings per share before extraordinary items. The dividend yield is the dividend per share divided by the closing price per share. The dividend yield is sensitive to share prices, whereas the dividend payout is not. For this reason, the dividend payout ratio is the primary measure of the firm's dividend payout in this study, and this is consistent with other studies (Smith and Watts, 1992; Gaver and Gaver, 1993; Gul, 1999 and Adam and Goyal, 2008; De Cesari and Ozkan, 2015; and Benjamin *et al.*, 2016).

3.3 Independent Variable

A primary measure of executive compensation (EXEC_COM) is the total compensation, including fixed salaries and variable bonuses (e.g., Larcker and Balkcom 1984; Antle and Smith, 1986; Alves *et al.*, 2016; Reddy *et al.*, 2015). In the U.K. and the U.S., disclosure of executive compensation of public listed firms is regulated through the Directors Report Regulation 2002 and the Sarbanes-Oxley Act 2002. However, in Malaysia, non-mandatory detailed disclosure is encouraged through guidelines specified by the MCCG issued by the Securities Commission in 2007, revised in 2012, and the latest revision in 2020. Thus, there is no specific regulation regarding directors' executive compensation disclosures in Malaysian PLCs. Hence, the data obtained for compensation consists of the salary and bonus earned annually[3].

3.4 Corporate Governance Variables

Remuneration committees play an essential role in advising the Board on matters relating to remuneration. As part of its function, the committee periodically makes recommendations to the Board on any specific decisions or actions and disclosures that the Board should consider with director remuneration (see Kanapathippillai *et al.*, 2016). In this study, the remuneration committee (REM_COM) consists of several independent directors in the remuneration committee board. Board composition (NED) refers to the number of non-executive directors who are external members of the Board. The ratio indicates the Board's

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[3] While compliance with the MCCG is not mandatory, amendments to the Bursa Malaysia listing rules in November 2017 means that listed companies in Malaysia would need to explain any non-compliance with governance standards in their annual report. With such requirements, the executive compensation disclosure is more detail post-2017.

independence and the extent to which insiders are not involved. Prior studies (i.e., Conyon and Peck, 1998; Nordin *et al.*, 2005; Ponnu, 2008; Lee and Isa, 2015; Benjamin and Zain, 2015) have identified external board members as non-executive have less power to control the Board of directors. One of the CEO characteristics of this study is the ' 'CEO's academic qualification (CEO_EDU). The criteria are indicated as zero if there is no specification of the academic qualification and one if a bachelor's degree and above. Board diversity is measured by the presence of majority Bumiputera (BUMI) directors coded as '1', and otherwise (i.e., Chinese, Indian, or others) coded as '0'.

3.5 Control Variables

We control for different firm-level variables. Board size (B_SIZE) refers to the total number of executive and non-executive directors on the Board. Prior studies suggest an association between the board size and the dividend payout performance (see Ajay, 2007; Lee and Isa, 2015; Benjamin and Zain, 2015). It makes sense, as large board members reflect the quality of corporate decision-making (Atayah *et al.*, 2021; Najaf *et al.*, 2021). CEO duality (CEO_Dual) is where the chief operating officer serves as the Board's chairman. This construct is a dummy variable, with firms scoring "1" if duality exists and "0" otherwise. Due to agency issues, the concentration of decision-making power at one point (CEO duality) would affect the dividend payout ratio (Chin *et al.*, 2021; Najaf *et al.*, 2020). The MBA ratio is the market-to-book value of assets at the end of year *t*. The computation is the total assets less total common equity and the market value of investment calculated as the share outstanding multiplied by a closing share price scaled by the total assets. Extant studies suggest that the MBA is one of the critical determinants of the dividend payout ratio. Returned earnings (RET_EAR) is the natural logarithm of retained earnings. The size (proxied as the natural log of total assets) and debt leverage (proxy as nature log of total liabilities to total assets) of the firms has a significant association with the dividend payout ratio (Najaf and Najaf, 2021). Government-linked companies (GLCs) refer to a dummy variable coded as '1' when the firm is identified as a government-link company and '0' otherwise. GLC control firms (FLY_C) refers to dichotomous variable coded '1' when the firm is recognized as a family own and '0' otherwise. A firm is categorized as a family firm if 20% or more equity ownership lies with the family or holds more board seats than any other individual or group on the Board. Institutional Ownership (INST) represents the percentage of shares held by all other institutional investors (excluding Employers Provident Fund (EPF), Lembaga Tabung Haji Angkatan Tentera (LTAT), Permodelan Nasional Berhad (PNB), Lembaga Tabung Haji (LTH), and Social Security Organization (SOCSO) holding at least 5 percent of outstanding shares (Najaf *et al.*, 2021; Najaf and Atayah, 2021).

The ownership structure in Malaysia is highly concentrated. Hence, the relevant agency problem to analyse seems to be the one that arises from the conflicting interests of large shareholders and minority shareholders, eventually affecting the firm's dividend payout. All the variables have been winsorized at the 1 percent and 99 percentiles to avoid the effect of outliers. Furthermore, we control for the industry and year effects.

3.6 Model Specifications

The base Model tests hypotheses H1-H5 and Model 1 test hypotheses H5b, respectively. The regression model used to test the premises is as follows:

3.6.1 Base Model

$$DIV\_POUT_{i,t} = \beta_0 + \beta_1 EXEC\_COM_{i,t} + \beta_2 REM\_COM_{i,t} + \beta_3 BUMI_{i,t} + \beta_4 NED_{i,t}$$
$$+ \beta_5 CEO\_EDU_{i,t} + \beta_6 B\_SIZE_{i,t} + \beta_7 CEO\_DUAL_{i,t} + \beta_8 MBA_{i,t}$$
$$+ \beta_9 T\_ASSETS_{i,t} + \beta_{10} LEV_{i,t} + \beta_{11} RET\_EAR_{i,t} + \beta_{12} GLC_{i,t}$$
$$+ \beta_{13} FLY\_C_{i,t} + \beta_{14} INST_{i,t} + \beta_{15} IND\_DUM_{i,t} + \beta_{16} YR\_DUM_{i,t} + \varepsilon_{i,t} \tag{1}$$

3.6.2 Model 1 (with interactions)

$$DIV\_POUT_{i,t} = \beta_0 + \beta_1 EXEC\_COM_{i,t} + \beta_2 REM\_COM_{i,t} + \beta_3 BUMI_{i,t} + \beta_4 NED_{i,t}$$
$$+ \beta_5 CEO\_EDU_{i,t} + \beta_6 B\_SIZE_{i,t} + \beta_7 CEO\_DUAL_{i,t} + \beta_8 MBA_{i,t}$$
$$+ \beta_9 T\_ASSETS_{i,t} + \beta_{10} LEV_{i,t} + \beta_{11} RET\_EAR_{i,t} + \beta_{12} GLC_{i,t}$$
$$+ \beta_{13} FLY\_C_{i,t} + \beta_{14} INST_{i,t} + \beta_{15} EXEC\_COM*BUMI_{i,t} \tag{2}$$
$$+ \beta_{16} IND\_DUM_{i,t} + \beta_{17} YR\_DUM_{i,t} + \varepsilon_{i,t}$$

4. Results

Table 2 provides descriptive statistics for the sample firms. The mean dividend payout (DIV_POUT) ratio is 1.33 percent, and the mean for the executive compensation (EXEC_COM) is 7.99 million per annum. The average board size (B_SIZE) is eight directors, and the number of firms with CEO duality (CEO_DUAL) is low at approximately 10 percent. The mean market-to-book ratio (MBA) is 2.32, the debt to total assets (LEV) ratio is 1.58 times, and the mean retained earnings (RET_EAR) is 8.22.

Table 2: Descriptive statistics for all sample firms for all years

Variable	N	Mean	Median	Std. Dev.	Min	Max
DIV_POUT	2,009	1.333	0.710	1.221	0.690	5.510
EXEC_COM	2,009	7.992	7.950	1.039	3.580	11.960
B_SIZE	2,009	8.429	8.000	2.206	3.000	18.000
CEO_DUAL	2,009	0.088	0.000	0.283	0.000	1.000
MBA	2,009	2.317	2.280	0.209	-2.680	4.470
T_ASSETS	2,009	7.424	7.230	1.556	2.560	13.370
LEV	2,009	1.578	1.500	0.512	1.020	8.860
RET_EAR	2,009	8.222	8.120	0.458	0.110	10.600
GLC	2,009	0.052	0.000	0.223	0.000	1.000
FLY_C	2,009	0.268	0.000	0.443	0.000	1.000
INST	2,009	6.061	0.950	11.893	0.000	75.240
REM_COM	2,009	2.180	2.000	1.190	0.000	7.000
BUMI	2,009	0.302	0.000	0.459	0.000	1.000
NED	2,009	5.740	6.000	2.240	0.000	14.000
CEO_EDU	2,009	2.143	2.000	0.676	1.000	3.000

Notes: The definition and measurement of dependent, experimental, and control variables appear in Appendix A.

The results show that the mean ownership of GLCs is approximately 5 percent, whereas the family shareholdings are roughly 27 percent. In addition, the average institutional shareholdings (INST) are about 6 percent. The remuneration committee ranges from zero to a maximum of 8 members with an average mean of 2 independent directors on the Board. The mean average of Bumiputera members is 30 percent. Furthermore, the mean percentage of non-executive directors on the Board is six members, with a maximum of 14 non-executive members. On average, there are at least two directors with a qualification of a degree and above. Refer to Appendix A for the variable labels, definitions, and measurements. Table 3 shows the correlation matrix between the variables, and multicollinearity is absent.

Table 3: Pearson correlations matrix for all sample firms for all the years

Variables	DIV_POUT	EXEC_COM	B_SIZE	MBA	T_ASSETS	LEV	RET_EAR	INST	REM_COM	NED
DIV_POUT	1.00									
EXEC_COM	0.06***	1.00								
B_SIZE	0.04**	0.29***	1.00							
MBA	0.12***	-0.04*	-0.06***	1.00						
T_ASSETS	0.03	0.42***	0.29***	-0.06***	1.00					
LEV	-0.04*	0.12***	0.02	-0.00	0.23***	1.00				
RET_EAR	0.08***	0.33***	0.18***	0.02	0.58***	0.06***	1.00			
INST	-0.04*	0.03	0.05***	0.00	0.25***	0.10***	0.11***	1.00		
REM_COM	0.05**	0.06***	0.12***	0.03	0.10*** *	0.03	0.06***	0.03	1.00	
NED	0.05**	0.03	0.68***	0.00	0.37***	0.05**	0.20***	0.15***	0.16***	1.00

Notes: ***Significant at 1% level, ** Significant at 5% level, * Significant at 10% level. Appendix A describes the variable labels and definitions.

Table 4: OLS Regression of dividend payout on directors compensation and control variables

Dependent variable DIVIDEND PAYOUT	Model 1	Model 2	Model 3	Model 4
Independent Variable				
EXEC_COM	0.046**	0.046**	0.050***	0.050***
	(0.019)	(0.019)	(0.019)	(0.019)
Control Variables				
B_SIZE	-0.082	-0.087	-0.091	-0.075
	(0.065)	(0.065)	(0.065)	(0.064)
CEO_DUAL	0.034	0.035	0.051	0.044
	(0.060)	(0.060)	(0.060)	(0.059)
MBA	0.527***	0.524***	0.523***	0.515***
	(0.170)	(0.169)	(0.166)	(0.170)
T_ASSETS	-0.012	-0.012	-0.023	-0.014
	(0.017)	(0.017)	(0.017)	(0.017)
LEV	-0.125***	-0.125***	-0.121***	-0.129***
	(0.041)	(0.041)	(0.041)	(0.041)
RET_EAR	0.123**	0.122**	0.122**	0.113**
	(0.055)	(0.054)	(0.054)	(0.053)
GLC	0.180**	0.175**	0.165*	0.185**
	(0.086)	(0.086)	(0.087)	(0.086)
FLY_C	0.090**	0.091**	0.103***	0.098***
	(0.038)	(0.038)	(0.038)	(0.038)
INST	0.002	0.002	0.002	0.002
	(0.001)	(0.001)	(0.001)	(0.001)
Corporate Governance				
REM_COM		0.031		
		(0.035)		
NED			0.020**	
			(0.009)	
CEO_EDU				0.053**
				(0.026)
BUMI				
EXEC_COM*BUMI				
Constant	-1.444***	-1.447***	-1.483***	-1.474***
	(0.559)	(0.557)	(0.550)	(0.551)
N	2,009	2,009	2,009	2,009
R-squared	0.623	0.623	0.624	0.624

Notes: The reported *t-statistics* in parentheses are the robust standard errors adjusted for clustering by firm and year. The definition and measurement of dependent, experimental, and control variables are in Appendix A. The subscripts ***, **, and *denote the 1 and 10% significance levels, respectively.

Hypothesis 1 (H_1) states that dividend payout is negatively associated with executive compensation; however, Table 4 regression results show that dividend payout is positively and significantly associated with directors' executive compensation (Models 1-7) at $p < 0.05$ level. As shown in Table 4 (Model 1-7), higher payment leads to significantly higher dividend payout, and the basic model explains 62.3 percent of the determinants of dividend payout. This positive relationship consistently holds in (Models 1-7) that controls for board governance. Thus, our results are not consistent with the findings of Bhattacharyya *et al*. (2008), as executive compensation in Malaysian PLCs is positively associated with dividend payout and hence demonstrating a contrasting view to the advanced theory of the agency paradigm between an emerging and a developed market. Accordingly, our results do not support H_1.

Table 4 *(continued)*

Dependent variable DIVIDEND PAYOUT	Model 5	Model 6	Model 7
Independent Variable			
EXEC_COM	0.049**	0.067***	0.071***
	(0.019)	(0.021)	(0.021)
Control Variables			
B_SIZE	-0.091	-0.098	-0.101
	(0.065)	(0.065)	(0.065)
CEO_DUAL	0.048	0.043	0.061
	(0.060)	(0.060)	(0.060)
MBA	0.516***	0.506***	0.495***
	(0.169)	(0.166)	(0.162)
T_ASSETS	-0.017	-0.015	-0.025
	(0.017)	(0.017)	(0.017)
LEV	-0.123***	-0.121***	-0.123***
	(0.041)	(0.041)	(0.041)
RET_EAR	0.115**	0.117**	0.110**
	(0.054)	(0.054)	(0.053)
GLC	0.155*	0.135	0.133
	(0.087)	(0.087)	(0.088)
FLY_C	0.097**	0.092**	0.110***
	(0.038)	(0.038)	(0.038)
INST	0.002	0.002	0.002
	(0.001)	(0.001)	(0.001)
Corporate Governance			
REM_COM			0.029
			(0.036)
NED			0.017**
			(0.008)
CEO_EDU			0.048*
			(0.027)
BUMI	0.073*	0.635**	0.604**
	(0.041)	(0.300)	(0.302)
EXEC_COM*BUMI		-0.070*	-0.070*
		(0.037)	(0.038)
Constant	-1.352**	-1.481***	-1.578***
	(0.557)	(0.555)	(0.541)
N	2,009	2,009	2,009
R-squared	0.623	0.624	0.626

Notes: The reported *t-statistics* in parentheses are the robust standard errors adjusted for clustering by firm and year. The definition and measurement of dependent, experimental, and control variables are in Appendix A. The subscripts ***, **, and *denote the 1 and 10% significance levels, respectively.

Hypothesis 2 (H_2) states a positive association between the remuneration committee (REM_COM) and dividend payout in Malaysian PLCs. However, the results in Table 4 (Model 3 and 7) show that the independence of the remuneration committee is not significant in influencing dividend decisions and hence does not provide support in linking the remuneration committee to the dividend distribution of Malaysian PLCs. We envisaged that as the remuneration committee is customarily made up of CEOs of a particular firm, they are influential in determining the firm's direction and their payouts to shareholders. Thus, our results do not support H_2.

Hypothesis 3 (H_3) states an association between CEO education and dividend payout, and our results indicate a positive and significant association at $p < 0.05$ level. The coefficient is 0.053, meaning that CEOs with at least a bachelor's degree tend to pay on

average 5.3 percent higher dividends than CEOs who have no university education, given that other explanatory variables are held constant. Hence, directors' compensation is commensurate with the CEO's level of education and earns higher pay with a higher dividend payout. However, on the other hand, this suggests that the CEO without postgraduate qualifications could trade off the return to shareholders with more top directors' remuneration that will directly benefit the executive directors and its senior management (Table 4 – Models 4 and 7).

We find a significant positive relationship at $p < 0.05$ level (Table 4 – Models 3 and 7). Hence, Hypothesis 4 (H_4) is supported and shows that board size or a high number of independent directors (both indicate good board governance) increases the likelihood of higher dividend payout. Hence, this study finds that non-state-controlled firms and firms with independent directors on the Board are more likely to remove CEOs underperforming.

Hypothesis H_5 states that a Bumiputera director on the Board is associated with a dividend payout of PLCs (Table 4 – Model 5). The BUMI variable is significantly and positively associated with the $p < 0.1$ level dividend payout. Nazri *et al.* (2012) opine that the government persuades Bumiputera firms to place Bumiputera directors on the firms' boards to increase the participation of Bumiputera in the corporate sector. In return, Bumiputera firms will be granted favours ' from the government in the form of loans from the banking sector at preferential prices to help them stabilize their capital base and penetrate capital markets. Under this situation, the firms are less likely to encounter financial problems when future investment opportunities arise because they will be bailout by the government. Hence, we expect Bumiputera directors' decisions to favour paying the extra cash flows as dividends to shareholders instead of Chinese directors. Thus, we conclude that the results support hypothesis H5, supporting the conviction that Bumiputera directors on the Board of Malaysian PLCs increase dividend payout.

Further, hypothesis H_{5a} relates to the association between dividend payout and executive compensation and how the Bumiputera directors on the Board moderate the relationship. This variable is negatively significant at $p < 0.10$ level, indicating that Bumiputera's correspond with lesser executive compensation.

4.1 Robustness Test

In the previous section, we have used dividend payout based on year-to-year. But one can argue that the dividend payout should be regressed with prior year directors' remunerations to prove causality. Furthermore, the dividend is declared after the Board approves the directors' compensation, which typically only happens after the financial year. Thus, we run the regression based on one-year ahead dividend payout against existing independent and control variables (by inserting Stata's convention for leads (F1, F2), before a variable leap it by one period/year ahead) using the following regression:

$$
\begin{aligned}
\text{F.DIV\_POUT}_{it+1} = {} & \beta_0 + \beta_1 \text{EXEC\_COM}_{i,t} + \beta_2 \text{REM\_COM}_{i,t} + \beta_3 \text{BUMI}_{i,t} \\
& + \beta_4 \text{NED}_{i,t} + \beta_5 \text{CEO\_EDU}_{i,t} + \beta_6 \text{B\_SIZE}_{i,t} + \beta_7 \text{CEO\_DUAL}_{i,t} \\
& + \beta_8 \text{MBA}_{i,t} + \beta_9 \text{T\_ASSETS}_{i,t} + \beta_{10} \text{LEV}_{i,t} + \beta_{11} \text{RET\_EAR}_{i,t} \qquad (3) \\
& + \beta_{12} \text{GLC}_{i,t} + \beta_{13} \text{FLY\_C}_{i,t} + \beta_{14} \text{INST}_{i,t} + \beta_{15} \text{IND\_DUM}_{i,t} \\
& + \beta_{16} \text{YR\_DUM}_{i,t} + \varepsilon_{i,t}
\end{aligned}
$$

We have run several robustness tests. Firstly, as the final dividend is declared after the Board approves the 'directors' compensation, which typically only happens after the financial year-end, we run the regression based on one-year-ahead dividend payout against the existing independent and control variables regression model as shown above. We use lag one-year and lag two-year dividend payout against existing independent and control

variables. Thus, we find that both prior year and two-year dividend payout lags (not shown here for brevity reasons) have no significant results demonstrating that the executive compensation has no effects on the dividend payouts of Malaysian PLCs. The White test establishes that the variance of the errors in the regression model is constant and not significant.

Nevertheless, when we split the sample into GLC and non-GLC firms (Table 5), the correlation between remuneration and performance is weaker in state-controlled firms. Similarly, when we divide the samples into FLY_C and non-FLY_C (Table 6), the relationship between remuneration and performance is more substantial for non-FLY_C. Hence, the result shows that the increase in the executive remuneration for state control and family control has no impact on the dividend payout. We foresee this unswerving for state control firms, which may have lower corporate governance, leading to lower operating performance and lower dividend payout or none. On the other hand, family control firms may have different business operation priorities and future growth.

Table 5: OLS regression results in GLC and NON-GLC

Dependent Variable	MODEL 1	MODEL 2
DIVIDEND PAYOUT	GLC	NON_GLC
Independent Variable		
EXEC_COM	-0.113	0.060***
	(0.112)	(0.020)
Control Variable		
B_SIZE	-0.339	-0.093
	(0.288)	(0.066)
CEO_DUAL	-	0.063
		(0.060)
MBA	0.267	0.497***
	(0.333)	(0.172)
T_ASSETS	0.047	-0.025
	(0.121)	(0.018)
LEV	-0.505	-0.109***
	(0.383)	(0.041)
RET_EAR	-0.267	0.112**
	(0.269)	(0.055)
FLY_C	-	0.116***
		(0.038)
INST	0.010**	0.001
	(0.004)	(0.001)
Corporate Governance		
REM_COM	-0.272	0.035
	(0.266)	(0.036)
BUMI	-0.014	0.034
	(0.246)	(0.043)
NED	0.028	0.021**
	(0.033)	(0.009)
CEO_EDU	-0.227	0.050*
	(0.187)	(0.027)
Constant	4.911*	-1.563***
	(2.626)	(0.559)
Number of Companies	15	272
N	105	1,904
R-squared	0.791	0.619

Notes: The reported *t-statistics* in parentheses are the robust standard errors adjusted for clustering by firm and year. The definition and measurement of dependent, experimental, and control variables are in Appendix A. The subscripts ***, **, and *denote the 1, 5, and 10% significance levels, respectively.

Table 6: OLS regression results FLY_C and NON-FLY_C

Dependent Variable DIVIDEND PAYOUT	MODEL 1 FLY_C	MODLE 2 NON-FLY_C
Independent Variable		
EXEC_COM	0.036	0.072***
	(0.035)	(0.024)
Control Variable		
B_SIZE	-0.128	-0.063
	(0.099)	(0.082)
CEO_DUAL	-0.026	0.165**
	(0.088)	(0.080)
MBA	0.453**	0.511***
	(0.217)	(0.182)
T_ASSETS	-0.0119	-0.035*
	(0.035)	(0.020)
LEV	-0.308***	-0.085*
	(0.086)	(0.045)
RET_EAR	0.137	0.120**
	(0.114)	(0.061)
GLC	-	0.157*
		(0.091)
INST	0.000	0.001
	(0.005)	(0.002)
Corporate Governance		
REM_COM	0.052	0.012
	(0.065)	(0.044)
BUMI	-0.117	0.095*
	(0.081)	(0.051)
NED	0.013	0.018*
	(0.017)	(0.010)
CEO_EDU	0.081*	0.045
	(0.047)	(0.033)
Constant	-1.196	-1.722***
	(0.927)	(0.646)
Number of Companies	77	210
N	539	1,470
R-squared	0.748	0.585

Notes: The reported *t-statistics* in parentheses are the robust standard errors adjusted for clustering by firm and year. The definition and measurement of dependent, experimental, and control variables are in Appendix A. The subscripts ***, **, and *denote the 1, 5, and 10% significance levels, respectively.

5. Conclusion

In developed countries, regulatory reforms and stock exchange requirements have attempted to regulate executive pay to be consistent with firm performance over the decades. For example, by stipulating that all or most of the directors on a company's Board who set compensation must be independent, each year, firms must reveal the size and structure of their top executives' compensation and the reasoning behind it. As a result, CEOs and their boards know what their peers are making, but critics say boards use that information in a dysfunctional manner to ratchet up overall pay.

Hence, dividend payout and CEO compensation are puzzling research areas as there are few studies of such a relationship, especially in a developing country context such as Malaysia. Furthermore, the advent of several corporate governance measures proposed under the MCCG makes our study comprehensive. Our results are not consistent with

Bhattacharyya *et al.*'s (2011) findings that executive compensation is negatively associated with dividend payout.

This study also shows that CEO education is commensurate with the dividend payout, an essential factor determining the dividend payout in Malaysia. Consistent with agency theory, the lower-paid CEO (compared to the higher-paid CEO with postgraduate qualifications) will endorse a lower dividend payout. However, when these CEOs receive a higher remuneration package, they will support a higher dividend payout rate. Furthermore, the additional factor influencing board composition (NEDs) in Malaysia is how the directors are independent of the firm's management. Rashidah and Roszaini (2005) posit that more independent directors' representation on the Board does not limit a firm's earnings management practices. Sharma (2011) opines that after controlling for the effects of traditional economic, CEO entrenchment, and ownership determinants of the propensity to pay dividends, there is evidence of a positive association between the tendency to pay and board independence.

Haniffa and Hudaib (2006) and Yatim *et al*. (2006) posit that ethnicity in Malaysia has, to a considerable extent, shaped how the country and businesses are managed due to external political intervention and internally via its cultural values. The political economy of Malaysia, where critical government support to the GLCs has fostered the emergence of a new class of the indigenous local capitalist class, is increasing structures of class and ethnicity (Larson and Zalanga, 2003). Our results find support for Iskandar *et al.* (2017) that Bumiputera's on boards can positively impact dividend payout. This effect may be conditional on the level of free cash flows generated by firms. Furthermore, in the interaction between executive compensation and Bumiputera, dividend payout is weaker with the existence of Bumiputera. This result has policy implications for ethnicity as an active board governance mechanism. In an emerging capital market like Malaysia, the results suggest that trying a formulaic approach to governance reform to optimize the link between executive compensation and dividends is not simple. The results show a negative and insignificant association between GLCs and executive compensation, suggesting that directors in GLCs appointed or seconded from civil service assume positions in the government pay schemes affect the link between executive pay and firm performance. On the other hand, family firms are evidence of lower executive compensation as family control reduces the vertical agency conflict between managers and shareholders.

This study's limitations include selecting only the top 300 highest capitalized Malaysian public listed companies, meaning that the study's conclusions might only be valid and applicable to large companies listed in Malaysia. The sample is also significantly influenced by its Islamic culture and associated biases. The research is in the positivist paradigm, and it should not be construed as a comment about a particular religion or race and relied mainly on a quantitative research approach. An important area for future research might be considering how shareholders' returns and executive compensations affect dividend payout in other emerging capital markets with different constitutional backgrounds, such as Chile, with a civil law jurisdiction.

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Appendix

Appendix A: Variable measurement

Variable	Descriptions
Dependent Variable	
DIV_POUT	The dividend payout ratio is the dividend per share scaled by earnings per share before extraordinary shares. The dividend payout is in the natural logarithm.
Independent Variable	
EXEC_COM	The aggregated pay of all executive directors on each firm is the sum of salary, bonus, and other cash payments
Corporate Governance	
REM_COM	The number of independent directors in the remuneration committee board.
BUMI	Dichotomous with one if BUMI, 0 if Chinese, Indian, and others
NED	The proportion of non-executive directors (NEDs) on the Board
CEO_EDU	CEO education is the academic qualification of the CEO of the firm. Criteria are indicated as 0 if there is no specification and one if a bachelor's degree and above.
Control Variables	
B_SIZE	A total number of directors on the Board of the company
CEO_DUAL	Dichotomous with one if the chairman is also the CEO of the company.
MBA	Market to book value of assets at the end of year t [(Total assets less total common equity add share outstanding multiplied by closing share price)/ total assets.]
T_ASSETS	Natural logarithm of total assets.
LEV	Natural logarithm of total liabilities over total assets
RET_EAR	Natural logarithm of Retained earnings
GLC	A dummy variable is coded as 1 when the firm is a government-link company and 0 otherwise
FLY_C	Dichotomous variable coded 1 when the firm is a family own, and 0 otherwise. A firm is categorized as a family firm if 20% or more equity ownership lies with the family or holds more board seats than any other individual or group on the Board.
INST	The percentage of shares held by all other institutional investors (excluding EPF, LTAT, PNB, LTH, and PERKESO/SOCSO) containing at least 5 percent of outstanding shares)
IND _DUM	Dummy variable coded 1 for the specific Industry, 0 otherwise.
YR _DUM	Dummy variable equals 1 for the specific year, 0 otherwise.