Journal of Behavioral and Experimental Finance 3 (2014) 22–40

Contents lists available at ScienceDirect

Journal of Behavioral and Experimental Finance

journal homepage: www.elsevier.com/locate/jbef

Full length article

National culture and dividend policy: International evidence from banking☆

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ARTICLE INFO

Article history:
Received 25 April 2014
Received in revised form 27 June 2014
Accepted 21 July 2014
Available online 13 August 2014

JEL classification:
G2
G35

Keywords:
Banking
Dividend policy
National culture
Uncertainty avoidance
Masculinity
Long-term orientation

ABSTRACT

We examine the relations between three dimensions of national culture and dividend policies of banks using a sample of banks from 51 countries over the period 1998–2007. In our main analysis, we employ three dimensions of Hofstede et al. (2010) and find that banks in high uncertainty avoidance, high long-term orientation and low masculinity countries pay lower amount of dividends and, are less likely to pay dividends. To confirm our main results, we also employ comparable three dimensions of national culture of House et al. (2004) and find that banks in high uncertainty avoidance, high future orientation and low assertiveness countries pay lower amount of dividends and, are less likely to pay dividends, findings confirming our above results. In sum, we find significant influence of the three dimensions of national culture on bank dividend policies.

1. Introduction

We employ three dimensions of national culture from two culture measuring studies of Hofstede et al. (2010) and House et al. (2004), and an international sample of banks to study the effects of national culture on bank dividend policies. Cross-country differences in banks' propensity to pay dividends and level of dividend payments are likely to be affected by differences in corporate governance and legal institutions, as well by softer dimensions such as national culture that may influence excessive earnings retention or payment as dividends.

The extant literature has studied the relation between national culture and dividend policies, but has excluded banking firms (Khambata and Liu, 2005; Shao et al., 2009; Fidrmuc and Jacob, 2010; Bae et al., 2012). A large amount of literature has documented that financial systems promote economic growth by mobilizing savings, reducing information asymmetries, providing risk-sharing and facilitating exchange (Levine, 1997, 2005; Hassan et al., 2011). Due to such an important role performed by this highly leveraged industry for national economies and quite different nature of banking firms as compared to industrial firms, it is important to examine the relation of cultural forces with bank dividend policies. Further, numerous studies have examined the bank dividend policies separately from the dividend policies of industrial firms (Casey and Dickens, 2000; Dickens et al., 2002; Theis and Dutta, 2009).

☆ This paper is funded by the project of National Natural Science Foundation of China (NSFC) (Grant # 71173077). We thank the editor, Brian Lucey, and the anonymous referees for their very constructive comments.

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http://dx.doi.org/10.1016/j.jbef.2014.07.002
2214-6350/

In addition, more cash holdings can encourage bank managers to take more risk by extending poor credit quality loans. In a global survey on factors that created the conditions for the banking crisis conducted in May 2008 by Economist Intelligence Unit and PricewaterhouseCoopers, 58% of survey participants put the blame on 'ineffective regulatory oversight', 31% on 'monetary policy', and an impressive 73% on 'culture and excessive risk-taking' (Kanagaretnam et al., 2011). Cross-country differences became more apparent in the recent financial crisis, which had a significantly larger adverse effect on banks in certain countries (e.g., the UK and the USA) than in others (e.g., Australia and Canada). Given these findings, an examination of the influence of national culture on bank dividend policies is clearly warranted.

Culture is generally defined as a set of norms, beliefs, expected behaviors and shared values that serves as guiding principles in people's lives (Schwartz, 1994; Hofstede, 2001). By guiding human behavior, cultural values reflect what a society/group considers to be legitimate or illegitimate, good or bad, acceptable or unacceptable, or ethical or unethical (Hofstede, 2001). On the other hand, extant literature argues the important role of dividend policies in reducing agency costs and minimizing information asymmetries (Rozeff, 1982; Easterbrook, 1984; La Porta et al., 2000; Denis and Osobov, 2008; Eije and Megginson, 2008; Brockman and Unlu, 2009). And, in a recent study, John et al. (2010) argue that agency costs are more severe in banks due to their higher leverage. Therefore, we base our theoretical framework on Fidrmuc and Jacob (2010) who offer an agency theory based explanation of dividends for national cultural dimensions. This approach considers the preferences and behaviors of economic agents inherent in the cultural values for determining dividend policies of firms. So, in this paper we argue that bank dividend policies are a special case of social norms reflecting the legitimacy or acceptability of certain dividend payout strategies in a society. Across countries, social norms governing dividend payout policies may vary because differing cultural value emphases breed different behaviors, aspirations, beliefs, and preferences, and therefore alter the severity and nature of agency conflicts.

An alternative view is that because banks operate in highly regulated environments, and are strictly monitored by central banks for capital levels, therefore, country-level national cultural factors may not be as important in influencing bank dividend policies. In this regard, banks may face different levels of regulatory pressure both at bank- and country-levels. On bank-level, low capitalized banks can be under severe regulatory pressure for increasing capital by not paying dividends than the banks which either meet regulatory capital requirements or operate with the capital levels significantly above regulatory minimum requirements. Similarly, on country-level, banks in some countries may face more stringent capital requirements than the banks in other countries which have less stringent capital requirements. If we find significant cultural effects on bank dividend policies after controlling for bank- and country-level regulatory pressure, then we can argue that cultural forces are even more important for other less-regulated or un-regulated industries.

Bae et al. (2012) hypothesize and find that national culture influences dividend policies of nonfinancial firms. More specifically, they document that three dimensions of national culture – uncertainty avoidance, masculinity and long-term orientation – have negative relations with dividend payout amounts. Given their findings, we examine the relations between same three dimensions[2] of national culture, and bank dividend policies. We focus on the pre-financial crisis period (e.g., the period 1998–2007) in our analysis.

We derive three hypotheses based on three dimensions of national culture. First, we posit that bank insiders and outside shareholders in high uncertainty avoidance societies put heavy emphasis on the certainty that dividend payment expectations are met each period. Also, uncertainty-avert minority shareholders and bank insiders may prefer higher retained profits because they are cash resources to hedge against unforeseen financial distress. Therefore, we expect lower dividend payouts in high uncertainty avoidance societies. Second, we conjecture that in masculine cultures, agency conflicts are inherently more severe because their members are considered competitive and impatient, and are more prone to pursue opportunistic behavior rather than adhere to others' decisions and preferences. Therefore, outside shareholders are expected to demand higher level of dividends to discipline the opportunistic behavior of bank insiders. Finally, we hypothesize that in more long-term orientation countries, which tend to show greater perseverance, thrift and patience, the severity of agency conflicts is inherently lower. Consequently, investors have a lower preference for dividends as a disciplining mechanism and find lower dividend payouts culturally more acceptable.

We employ common dividends paid to total assets ratio and a dummy variable, equal to one for dividend paying banks and zero otherwise, to test the relations between three dimensions of national culture, and dividend payout amounts and the propensity to pay dividends, respectively.

We use an international sample of banks from *Bankscope* database representing 51 countries over the period 1998–2007 to test our predictions about cultural dimensions and bank dividend policies. We begin by examining the impact of cultural dimensions on dividend payout amounts while controlling for bank- and country-level regulatory pressure, bank size, profitability, asset growth, minority shareholder rights, creditor rights and level of financial market development. At bank-level, we use equity to total assets ratio of each bank to control for regulatory pressure because well capitalized (weakly capitalized) banks may face lower regulatory pressure (higher regulatory pressure) while deciding about dividend payments. At country-level, bank regulators in some countries may impose more stringent capital requirements for banks and then force banks to meet capital requirements before paying any dividends. Therefore, we use regulatory capital index of Barth et al. (2013) to account for cross-country heterogeneity in capital requirements and regulatory pressure.

2 We use updated version of long-term orientation from Hofstede and Minkov (2010).