

# THE EFFECT OF FREE CASH FLOW ON ASSET UTILIZATION WITH OWNERSHIP STRUCTURES AS MODERATING VARIABLES

**Elizabeth Nathania**  
Universitas Prasetiya Mulya  
[elizabeth.nathania@student.pmsbe.ac.id](mailto:elizabeth.nathania@student.pmsbe.ac.id)

**Samuel Putera**  
Universitas Prasetiya Mulya  
[samuel.putera@student.pmsbe.ac.id](mailto:samuel.putera@student.pmsbe.ac.id)

**Siti Farhana**  
Universitas Prasetiya Mulya  
[siti.farhana@pmsbe.ac.id](mailto:siti.farhana@pmsbe.ac.id)

**Wijantini**  
Universitas Prasetia Mulya  
[wijiyanti@pmsbe.ac.id](mailto:wijiyanti@pmsbe.ac.id)

## *Abstract*

*This study aims to examine how free cash flow (FCF) affects on asset utilization (AU) as a proxy for agency cost, followed by investigating the influence of ownership structures as moderating variables in reducing the negative effect of FCF on asset utilization. The research sample of 465 companies consisted of all companies listed on the Indonesia Stock Exchange in 2013-2017 with purposive sampling method. The findings of this study showed that FCF negatively influences AU). Institutional ownership weakens the negative relationship between FCF and AU. Contrarily, managerial ownership strengthens the negative relationship between FCF and AU. This study also found that family ownership strengthens the negative relationship between FCF and AU. This study contributes to understanding the role of various ownership structures in utilizing company's resources to improve their asset utilization, especially in the family ownership that dominates Indonesian firms.*

**Keywords:** *Asset Utilization, Family Ownership, Free Cash Flow, Institutional Ownership, Managerial Ownership*

## **INTRODUCTION**

Companies that are developing will tend to be faced with various agency problems, especially between management and shareholders. Companies that have substantive free cash flow can be one of the causes of agency problems (Wardhani, 2015). This is due to differences in interests between shareholders who want to use free cash flow for long-term investments, while managers tend to be opportunistic by

investing in projects that are profitable only for them.

A good governance structure is crucial in reducing agency costs arising from free cash flow, one structure of which is the presence of managerial and institutional ownership structures (Hadiprajitno, 2013). High managerial ownership can produce convergence between the interests of managers and shareholders (convergence of interest hypothesis). According to Bathala, Moon,

and Rao (1994), institutional shareholders can take the role of monitoring companies in overseeing management decisions through general meetings of shareholders. The impact is that management will be more careful and try to improve company performance. Family ownership is also very interesting to study, because the number of firm shares in Indonesia is mostly held by only a handful of families; namely 67% of open companies in Indonesia are family businesses (Claessens, Djankov, and Lang, 1999). In accordance with stewardship theory, management as well as family members who are controlling shareholders run the company not only for personal purposes, but for the long-term survival of the company (Davis, Donaldson, and Schoorman, 1997).

With the supervision and control of institutional ownership or convergence of interests brought by managerial ownership, management will be more efficient in utilizing company assets. Therefore, asset utilization is the agency cost proxy that is most appropriate to use in this study.

Javid, Malihi, and Soheilian (2014); Wang (2010); and Iskandar, Bukti, and Sanusi (2012) proved that the higher the free cash flow, asset utilization will be lower or inefficiencies will increase. It is also proven that managerial ownership and institutional ownership can weaken the negative relationship between free cash flow and asset utilization. Ang, Cole, and Lin (2000) proved that family ownership has lower agency costs. However, Kangarluei, Motavassel, and Abdollahi (2011); Khidmat and Rehman (2014); and Lin and Lin (2014) found the results of a positive FCF influence on company performance. Dewi and Nugrahanti (2014); Hadiprajitno (2013); Pratiwi and Yulianto, (2016) also found that managerial ownership and institutional ownership did not have a significant effect in reducing agency costs. Shleifer and Vishny (1997) found that family involvement in management may generate agency costs through managerial entrenchment. This proves that the level of

monitoring is still weak in reducing agency costs by managerial, institutional, and family ownership.

In addition to resolving the inconsistencies in the results of past studies, this study contributes to understanding the various ownership structures in reducing agency costs due to the high number of free cash flows, especially family ownership structures that have never been tested on samples of companies in Indonesia. In addition, research on agency costs with proxy asset utilization is still not done because the majority uses the ratio of expense to sales. The main objective of this study is to examine the relationship between free cash flow on asset utilization and to understand whether the relationship can be moderated by ownership structures, namely managerial ownership, institutional ownership, and family ownership.

## REVIEW OF LITERATURE AND HYPOTHESIS DEVELOPMENT

In general, developing companies experience agency problems. The agency problem arises because of an agency relationship within the company that involves the delegation of tasks to make decisions, from the principal / shareholders (the delegating party) to the agency / manager of the company (those who accept responsibility and provide services to the principal). The theory of agency contracts, commonly referred to as agency theory, is theorized by Jensen and Meckling (1976). According to Vidyantie and Handayani (2006), each person in the company is assumed to only act for their personal interests. Principals (shareholders) expect maximum returns in a fast period of time for the funds they invest. While the agent (manager) in making an investment will be opportunistic by using company funds on investment options that are in accordance with their preferences. This condition will trigger the emergence of agency costs.

One of the factors that cause agency problems is the use of free cash flow. Free cash flow in this context is defined as the

remaining cash flow to fund projects that have a positive NPV when discounted by the cost of relevant capital (Jensen, 1986). Free cash flow can be a measure of a company's financial performance. Without cash flow, new product development, acquisition processes, dividend payments, and debt repayments are difficult for every company (McClure, 2003).

However, according to the free cash flow hypothesis developed by Jensen (1986), managers who have large FCF tend to choose to invest in projects that have a negative NPV rather than having to be allocated to shareholders in the form of dividends. The tendency of manager's investment in investment occurs because of agency problems, where agents (managers) and principals (shareholders) have different interests. The manager's interests can be for empire building (manager only focuses on expanding firm size to gain prestige) or managerial entrenchment (manager expands the company to a direction that he only masters).

When the company's cash flow is excessive, manager inefficiencies in using FCF can also be triggered by the assumption of the Pecking Order Theory. In the pecking order theory, companies are assumed to prioritize the use of internal cash as a source of investment funding, rather than using debt or issuing new shares (Myers and Majluf, 1984). If the FCF in the company is excessive, managers can use internal cash to fund their investments, so that market control will be reduced because managers do not need to raise external funds. With this situation, where the manager can be more arbitrary in using funds for investment, thus leads to an increase in agency cost if the company has an excess of FCF.

As one of the mechanisms of corporate governance, the presence of ownership structures can reduce agency costs. The ownership structure that will be investigated further in this research is the structure of institutional, managerial, and family ownership. The institutional

ownership structure according to Nuraina (2012) is a share ownership by institutions, such as insurance companies, pension funds, investment companies, and other companies. Bathala et al. (1994) in his research proved that the presence of institutional ownership structures can minimize agency costs. In accordance with the efficient-monitoring hypothesis proposed by Pound (1988), the higher the level of institutional ownership, the institutional party will have more motives and voting rights in monitoring and controlling management decisions so as to provide better performance for the company (Pound, 1988). However, on the other hand when ownership of institutional investors gets bigger in the company, it can have a negative impact on the company through an alliance strategy with management to prioritize ownership of the majority shareholders (institutions). The alliance strategy will generally result in a company policy that is not optimal (Sujoko and Subyantoro, 2007).

Then there is the managerial ownership structure which is share ownership by the management of the company that has responsibility and is active in the decision making process. In this case the management is usually a director (Diyah and Widanar, 2009). Jensen and Meckling (1976) and Ang et al. (2008) proved that higher managerial ownership reduces the agency cost of the company. This is in accordance with the Convergence of Interest Hypothesis proposed by Morck, Shleifer, and Vishny (1998), which said when share ownership by managers is high, the agency cost in the company will decrease, because the interests of managers are in line with shareholders (which includes the managers themselves), which is to increase the value of the company.

But on the other hand, Morck et al. (1998) also revealed that the higher managerial ownership can also increase agency costs. This is in accordance with Entrenchment Hypothesis, which proclaims that managers will try to gather power for

corporate control so that they get the freedom to manage it according to their interests. With this hypothesis, Ellili (2012) argues that managers can protect themselves from dismissal, and the fact that managers can make shareholders trust and approve manager policies even though it has an impact on decreasing shareholder value.

As the ownership structure that dominates public companies in Indonesia, Job (2008) defines family ownership as individual ownership and closed companies (above 5%), excluding public companies, countries, or financial institutions. Companies with family share ownership not only obtain ownership by placing family members in management positions, but ownership can be obtained indirectly through certain institutions. Davis, Schoorman, Mayer, and Tan (2000) prove the existence of a positive relationship between family ownership and company value is in accordance with stewardship theory. This is because company leaders who are family members, in controlling the company are not driven by personal economic interests. They reflect the stewards of the company to realize the company's mission, give the best, and are willing to sacrifice personal interests for the long-term success of the company.

However, Claessens et al. (1999) prove that the presence of family ownership can lead to agency problems between majority and minority shareholders this phenomenon tends to occur in developing countries. With increasing in firm age, managerial entrenchment by family members is likely to occur thus even though they have no longer sufficient competencies in increasing firm value. In addition, managerial entrenchment can occur due to the family company being run altruistically and the existence of amoral familism which can reduce the effectiveness of monitoring so as to increase agency costs (Schulze, Lubatkin, Dino, and Buchholtz, 2001).

#### **Hypothesis Development**

**Free Cash Flow (FCF) and Asset Utilization (AU)**

When a company has sufficient amount of internal cash for investment, external fundraising is not necessary, so managers also do not need to provide detailed information to the public on the investment decisions they make. Low market control of companies can encourage managers to invest in projects that have a negative impact on the welfare of shareholders (Ferreira and Vilela, 2004). Companies that have excess cash reserves in times where investment opportunities in projects with positive net present value (NPV) are not available, tend to face higher agency problems. This is because FCF increases the conflict of interest between shareholders and managers (Jensen and Meckling, 1976).

Excessive FCF owned by the company also becomes a cause of over-investment (Jensen, 1986). This is because companies that expand excessively above optimal values and increase in company resources under management control can increase salaries and manager's strength and prestige, also called empire building phenomena (Jensen, 1986 and Stulz, 1990). However, if the company already has limited ability in and opportunity in growing, an increase in the size of the company that is excessive will actually harm the interests of shareholders. In addition, when faced with investment opportunities, managers tend to choose an investment strategy that is in accordance with their competencies and abilities, although it is not necessarily going to increase the value of the company, thus creating a dependency on the manager of the company. This phenomenon is called managerial entrenchment (Shleifer and Vishny, 1989). Therefore, it can be concluded when the FCF of the company is high, the agency costs of the company will increase or the AU will decrease.

H1. There is a negative relationship between Free Cash Flow and Asset Utilization.

**Institutional Ownership Structure moderates the relationship between Free**

### **Cash Flow (FCF) and Asset Utilization (AU)**

According to Davis (2002), monitoring of management performance can be done more efficiently and effectively by institutional investors than individual investors. They have expertise in evaluating company operational activities and have greater voting rights in taking corrective actions if necessary (Brown, Chen, and Shekhar, 2011). Monitoring by institutional investors will prevent managers from using the company's cash for capital expenditures which can reduce the value of the company. Institutional investors will encourage managers to act with long-term thinking so that the company continues to grow and not fall (Davis, 2002).

Wijayati (2015); Javid et al. (2014); and Iskandar et al. (2012) prove the positive significant effect between institutional ownership on asset utilization, so that the efficiency of the company increases with decreasing agency costs. It can be concluded that the presence of institutional ownership will encourage more effective monitoring of the use of the company's free cash flow so that it will have an impact on increasing asset utilization.

H2. If institutional ownership increases, the negative relationship between free cash flow and asset utilization is weakened.

### **Managerial Ownership Structure moderates the relationship between Free Cash Flow (FCF) and Asset Utilization (AU)**

The "convergence of interest" hypothesis states that the higher the level of managerial ownership, the interests of management and the interests of shareholders will be more integrated, thus reducing agency cost. Thus, a high level of management ownership can also improve company performance and asset utilization as an agency cost proxy (Singh and Davidson III, 2003 and Jensen, 1993;). Lin and Chang's (2008) research is also in line with this hypothesis, where his research proves that managerial ownership can mitigate principal-agent conflicts

(increasing the efficiency of asset utilization).

Management of companies with a high level of managerial ownership is more likely to use the FCF wisely and invest in projects that add value to the company, because doing so managers also add their own wealth (Lawal and Yero, 2016). It can be concluded, according to the convergence of interest hypothesis managers will spend FCF wiser so that asset utilization will increase.

H3. If managerial ownership increases, the negative relationship between free cash flow and asset utilization is weakened.

### **Family Ownership Structure in moderating the relationship between Free Cash Flow (FCF) and Asset Utilization (AU)**

Family ownership can reduce conflicts of interest between principals and agents. The higher the percentage of family ownership in a company, the effect on increasing the value of the company will be higher, this is because they want to be able to inherit the company to the next generation (Shleiver and Vishny, 1997). Similarly, Bhattacharya and Ravikumar (2001) stated that with family ownership, they tend to run their own business or appoint family members, and they care about the survival of the organization, not only during their lifetime, but also they care about the welfare of the next generation who will run their business.

This is in accordance with stewardship theory, where managers and shareholders in controlling a company are not driven by personal economic interests. The family as the owner and the one running the company, is intrinsically motivated to do the best for the company, realize the company's mission, and commit to making the company successful despite sacrificing personal interests. They tend to have a long-term perspective, especially in the decision-making process for increasing the value of the company because they have had a long relationship with the company. The research conducted by Hadiprajitno

(2013) proves that family ownership can increase the efficiency of a company with a proxy for asset turnover. It can be concluded that companies with family ownership can

use FCF wisely so that the efficiency reflected in the AU will increase.

H4. If there is family ownership, then the negative relationship between free cash flow and asset utilization is weakened.

## RESEARCH METHODS

### Regression Models

In testing the hypothesis, the author uses the unbalanced panel data type with the OLS

Model 1 to test hypothesis 1

$$ASSET\_UT_{it} = \alpha_0 + \alpha_1 FCF_{it-1} + \alpha_2 ROA_{it} + \alpha_3 SIZE_{it} + \alpha_4 LEV_{it} + \alpha_5 AS_{it} + \alpha_6 RISK_{it} + \alpha_7 AGE_{it} + \varepsilon$$

Model 2 to test hypothesis 2

$$ASSET\_UT_{it} = \alpha_0 + \alpha_1 FCF_{it-1} + \alpha_2 INS_{it} + \alpha_3 (FCF_{it-1} * INS_{it}) + \alpha_4 ROA_{it} + \alpha_5 SIZE_{it} + \alpha_6 LEV_{it} + \alpha_7 AS_{it} + \alpha_8 RISK_{it} + \alpha_9 AGE_{it} + \varepsilon$$

Model 3 to test hypothesis 3

$$ASSET\_UT_{it} = \alpha_0 + \alpha_1 FCF_{it-1} + \alpha_2 MAN_{it} + \alpha_3 (FCF_{it-1} * MAN_{it}) + \alpha_4 ROA_{it} + \alpha_5 SIZE_{it} + \alpha_6 LEV_{it} + \alpha_7 AS_{it} + \alpha_8 RISK_{it} + \alpha_9 AGE_{it} + \varepsilon$$

Model 4 to test hypothesis 4

$$ASSET\_UT_{it} = \alpha_0 + \alpha_1 FCF_{it-1} + \alpha_2 FAM_{it} + \alpha_3 (FCF_{it-1} * FAM_{it}) + \alpha_4 ROA_{it} + \alpha_5 SIZE_{it} + \alpha_6 LEV_{it} + \alpha_7 AS_{it} + \alpha_8 RISK_{it} + \alpha_9 AGE_{it} + \varepsilon$$

Pooled regression model. The following is a research regression model for the four hypotheses proposed in this study:

Description:

Asset_UT <sub>it</sub>	=	Asset Utilization
FCFit-1	=	Free Cash Flow
ROA <sub>it</sub>	=	Return on Assets
SIZE <sub>it</sub>	=	Company Size
LEV <sub>it</sub>	=	Total Debt / Total Assets
AS <sub>it</sub>	=	Asset Structure
RISK <sub>it</sub>	=	Risk of Company
AGE <sub>it</sub>	=	Company Age
INS <sub>it</sub>	=	Institutional Ownership
MAN <sub>it</sub>	=	Managerial Ownership
FAM <sub>it</sub>	=	Family Ownership
ε	=	Error
i	=	Number of Companies
t	=	Observation Year

## Operationalisation of Research Variables

**Table 1**  
**Operationalisation of Research Variables**

No	Variable	Definition	Proxy
<b>Dependent Variable</b>			
1	<i>Asset Utilization</i> (Asset_UT)	This study measures asset utilization by dividing total sales by total assets	$ASSET\_UT = \frac{Total\ Sales}{Total\ Asset}$
<b>Independent Variables</b>			
2	<i>Free Cash Flow</i> (FCF)	This measurement reflects a free cash flow available for short-term (working capital) and long-term investments (capital expenditure)	$FCF_{t-1} = \frac{EBIT_{t-1} + Dep_{t-1} - Tax_{t-1} - IExp_{t-1} - Div_{t-1}}{Total\ Sales_{t-1}}$ <p>Description:            EBIT = Income before interest and tax            Dep = Depreciation expenses            Tax = Tax Fee            IExp = Interest expense            Div = Dividend</p>
3	<i>Institutional Ownership</i> (INS)	At least 5% of shares held by an institutional or institution, such as insurance companies, pension funds, investment companies, and other companies at the end of the year. In this study the author specified the definition of institution that is purely an external public party, not an institution that has a family affiliation with the founder of the company	$INS_{it} = \frac{Number\ of\ Shares\ Owned\ by\ Institutional}{Total\ Shares} \times 100$
4	<i>Struktur Kepemilikan Manajerial</i> (MAN)	Share ownership of the management that is still active and responsible for taking part in decision making within the company. The author specified the definition of management that is purely an external party management, not management that has family affiliation with the	$MAN_{it} = \frac{Number\ of\ Shares\ Owned\ by\ Managerial}{Total\ Shares} \times 100$

No	Variable	Definition	Proxy
.		company's founder	
5	Struktur Kepemilikan Keluarga (FAM)	First criteria: founder and family member (from blood or marriage) have at least 10% ownership rights directly or indirectly. Second criteria: Namely family ownership traced to various layers of ownership of open companies (pyramid ownership structure).	Using dummy variable: 1 for family ownership company and 0 for non-family ownership company
<b>Control Variables</b>			
6	Profitability (ROA)	Return on Assets (ROA) generated from the percentage of net income divided by total assets	$ROA = \frac{Net\ Income}{Total\ Asset} \times 100$
7	Firm Size (SIZE)	Natural logarithms of total assets	$SIZE = \ln(Total\ Asset)$
8	Leverage (LEV)	Debt to Asset generated from total debt divided by total assets	$LEV = \frac{Total\ Debt}{Total\ Asset} \times 100$
9	Asset Structure (SA)	The total fixed assets divided by total assets which determines how much corporate funds are allocated to current assets and fixed assets.	$SA = \frac{Total\ Fixed\ Asset}{Total\ Asset}$
10	Firm Risk (RISK)	Standard deviation proxy for daily stock returns during the relevant financial year. Stock returns are defined as the daily current year's market index minus the previous year's daily market index divided by the previous year's daily market index.	$Return = \frac{Daily\ Market\ Index_n - Daily\ Market\ Index_{(n-1)}}{Daily\ Market\ Index_n}$ $Risk = StdDev(Return)$ <p>Description: StdDev = Standard Deviation</p>



No	Variable	Definition	Proxy
11	Firm Age (AGE)	Measured by the number of years since the establishment of the company	$AGE = Research\ Year - Year\ of\ Company's\ Establishment$

### Population and Sample

The population of this study is public companies in Indonesia that are listed on the IDX in the period 2013-2017. Sample selection is done by purposive sampling method with the criteria: excluding companies that are in the financial industry, companies that have just recorded IDX in

the year of the study are not excluded from the sample, and companies must have ownership structure data. Data is obtained from various sources, including: company annual reports, Bloomberg, IDX websites, and online news. The following is a calculation of the number of samples to be examined:

**Table 2**

### Sample Selection Procedure

Sample Selection Criteria	Total Company as Sample
Public company listed on the Indonesia Stock Exchange in 2013-2017	584
Companies in the Financial Industry	(100)
Companies that are delisted in 2013-2017	(19)
Total number of companies sampled	465

## RESULTS AND DISCUSSION

Tests on the four models using Pooled OLS driscoll-kraay standard errors in Stata to overcome the symptoms of heteroscedasticity and autocorrelation. Transformation data was used in order to deal with normality issue according to the criteria in the journal Tabachnick and Fidell (2007) and Howell (2007).

### Descriptive and Correlation Statistics

In table 3 below, it shows that the AU has a mean of 0.8204, which means that the average company in Indonesia employs its assets by 82% per period or every 1 rupiah in total assets can generate 0.8204 rupiah in total sales. The maximum AU value of 9,151 is the ratio owned by PT Renuka Coalindo, Tbk. in 2017. The FCF variable has a mean of 0.0055, indicating

that from one rupiah sales can generate 0.0055 rupiah free cash flow that can be invested the following year. The maximum value of 25,096 is owned by PT Bumi Resources Mineral, Tbk in 2017. The INS variable has a mean of 0.1431, meaning that the average company in Indonesia is owned by an institution with ownership of 14.31%. The highest institutional ownership is owned by PT HM Sampoerna at 98%. MAN variables have a mean of 0.0187 or the average managerial ownership in Indonesian companies is only 1.87%. The highest managerial ownership is owned by PT J Resources Asia Pacific at 94.6%. The mean FAM variable of 0.6865 shows that 68.65% of companies in Indonesia are controlled by families.

**Table 3**

Variabel	Obs	Descriptive Statistics			
		Mean	Std. Dev	Min	Max
AU	2089	0,8204	0,8299	0,000	9,151

FCF	2089	0,0055	1,4294	-32,801	25,096
INS	2089	0,1431	0,2469	0,000	0,980
MAN	2089	0,0187	0,0961	0,000	0,946
FAM	2089	0,6865	0,4640	0,000	1,000
ROA	2089	0,0181	0,2895	-10,744	2,192
SIZE	2089	8.225.172	19.429.669	5.081	295.831.324
LEV	2089	0,2801	0,5123	0,000	11,658
SA	2089	0,3962	0,2449	0,000	0,953
RISK	2089	0,0356	0,0321	0,000	1,012
AGE	2089	31,0397	16,7035	2	158

### Analysis of Regression Result

The four models are tested using Pooled OLS with discroll-kray standard errors method in Stata to overcome the symptoms of heteroscedasticity and autocorrelation.

Observation data have also been transformed to deal with normality issue according to the criteria proposed by Tabachnick and Fidell (2007) and Howell (2007).

**Table 4**  
**Results of Pooled OLS Regression**  
**Dependent Variable: AU**

Independent Variables	1 (n = 2089)	2 (n = 2089)	3 (n = 2089)	4 (n = 2089)
FCF	-0,0582 (0,002)***	-0,0658 (0,003)***	-0,0561 (0,002)***	-0,0263 (0,031)**
INS	-	-0,1255 (0,322)	-	-
MAN	-	-	0,5655 (0,003)***	-
FAM	-	-	-	0,0768 (0,005)***
FCF*INS	-	0,0904 (0,047)**	-	-
FCF*MAN	-	-	-0,5048 (0,005)***	-
FCF*FAM	-	-	-	-0,0569 (0,002)***
ROA	1,3150 (0,000)***	1,3282 (0,000)***	1,3139 (0,000)***	1,2974 (0,000)***
SIZE	-0,0417 (0,000)***	-0,0422 (0,000)***	-0,0414 (0,000)***	-0,0413 (0,000)***
LEV	0,7635 (0,021)**	0,7745 (0,016)**	0,7623 (0,020)**	0,7536 (0,012)**
SA	0,0608 (0,399)	0,0621 (0,380)	0,0550 (0,436)	0,0529 (0,479)
RISK	0,4835 (0,047)**	0,4865 (0,049)**	0,4774 (0,053)*	0,4638 (0,056)*
AGE	0,0051 (0,000)***	0,0052 (0,000)***	0,0052 (0,000)***	0,0052 (0,000)***
Konstanta	-0,0871 (0,280)	-0,0777 (0,271)	-0,0926 (0,270)	-0,1364 (0,172)

**Dependent Variable: AU**

<b>Independent Variables</b>	<b>1 (n = 2089)</b>	<b>2 (n = 2089)</b>	<b>3 (n = 2089)</b>	<b>4 (n = 2089)</b>
<b>Prob &gt; F</b>	0,0000	0,0001	0,0000	0,0001
<b>Adjusted R-squared</b>	0,1662	0,1673	0,1683	0,1774

Notes: \*\*\* significant at  $\alpha=1\%$ , \*\* significant at  $\alpha=5\%$ , \* significant at  $\alpha=10\%$

**Free Cash Flow (FCF) and Asset Utilization (AU)**

Second column in table 4, shows model 1 has an adjusted r-squared of 16.62%. Regression result of model 1 indicate that FCF has a significant negative effect on AU with p-value of 0.2%, so hypothesis 1 is proven. This result is consistent with the research conducted by Wang (2010), Javid et al. (2014), and Iskandar et al. (2012).

Free cash flow can be one of the causes of agency conflicts between shareholders and management (Wardhani, 2015). In accordance with the FCF theory developed by Jensen and Meckling (1976), that the company will be faced with a conflict of interest between shareholders and managers when the company has excess cash flow in times where there is no profitable investment opportunity. Wang (2010) proves that inefficiencies can arise as a result of the use of FCF that causes over-investment. This can happen because of the empire building phenomenon when managers try to continue to expand while there is no investment opportunity that will actually increase the size of the company, but not the value of the company (Jensen, 1986 and Stulz, 1990). Managerial entrenchment can also be another cause of inefficiency due to overinvestment, when managers tend to choose investments that are only in accordance with their abilities and competencies, although it is not necessarily going to increase the value of the company, which also creates dependence on the manager of the company (Shleifer and Vishny, 1989). This is in accordance with the research of Florackis and Ozkan (2006) which proves that managerial entrenchment has a significant negative relationship to asset utilization, this

can be due to the lack of effectiveness of monitoring and disciplinary mechanisms by controlling shareholders.

In accordance with the pecking order theory, low market control over the use of FCF companies can also be a cause of internal inefficiencies as a result of FCF misuse of investments (Ferreira and Vilela, 2004). This is because when a company has excessive internal cash, fundraising from external parties does not need to be done so the company does not need to convey detailed information on its investment decisions. With low external control, managers are more likely to abuse investment funds.

**Institutional Ownership Structure moderates the relationship between Free Cash Flow (FCF) and Asset Utilization (AU)**

Third column in table 4, shows model 2 has an adjusted r-squared of 16.73%. Regression result of model 2 depicts that FCF has a significant negative effect on AU with a p-value of 0.3%. FCF \* INS as a moderating variable has a significant positive effect on the AU dependent variable with a p-value of 4.7% so that hypothesis 2 is proven. Institutional shareholders proved to be able to weaken the negative relationship between FCF and the AU. This result is consistent with the research conducted by Brown et al. (2011), and according to the efficient-monitoring hypothesis.

Institutional investors can be more effective and efficient in monitoring management, because they have the ability to evaluate better and have greater voting rights for the company, thus reducing agency costs (Brown et al., 2011). Institutional monitoring can prevent management from using cash for bad

investments by reducing the extent of management discretion. More specifically, the results of the Lins (2003) study indicate that developing countries, including Indonesia, tend to have a low level of protection for shareholders, which can lead to poor governance due to lack of control from shareholders. With the existence of institutional ownership that takes the role of monitoring as a block shareholder, a poor governance structure due to the low level of protection can be covered.

***Managerial Ownership Structure moderates the relationship between Free Cash Flow (FCF) and Asset Utilization (AU)***

Fourth column in table 4, shows model 3 an adjusted r-squared of 16.83%. Regression result of model 3 explains that FCF has a significant negative effect on AU with a p-value of 0.2%. MAN variable shows a positive significant with p-value of 0.3%. FCF \* MAN as a moderating variable has a significant negative effect on the AU dependent variable with p-value of 0.5% so hypothesis 3 is not proven. Managerial shareholders are proven to strengthen the negative relationship between FCF and AU.

In the results of descriptive statistics, companies in Indonesia have a very low percentage of managerial ownership, which is only 1.87%. Based on the results of Simoneti and Gregoric's (2004) research on Slovenian companies, which said that if the proportion of managerial ownership was less than 16%, then the effect of ownership would be negative on firm value. The relationship becomes positive if ownership is above 16%, so there is a u-shaped effect on managerial ownership. In developing countries like Indonesia, external shareholders tend to be passive in decision making and supervision of managers. Although the proportion of share ownership held is still small, it is possible for managers to enjoy great power and control over entrenchment effects. This can be caused by managers who tend to use company funds for their personal interests, rather than to

make investments that can increase company value, so it increase agency costs (reduce asset utilization). Based on the u-shaped effect, managers may only act like real owners (care about company performance) when the proportion of their share ownership reaches a certain point, where the incentive effect of ownership is greater than the entrenchment effect. The results of this study are not in accordance with the convergence of interest hypothesis developed by Morck et al. (1998), that when high managerial ownership will increase the value of the company so that it can reduce agency cost.

***Family Ownership Structure moderates the relationship between Free Cash Flow (FCF) and Asset Utilization (AU)***

Fifth column in table 4, model 4 shows an adjusted r-squared of 17.74%. Regression analysis of model 4 indicates that FCF has a significant negative effect on AU with a p-value of 3.1%. FCF \* FAM as a moderating variable has a significant negative effect on the AU dependent variable with a p-value of 7.8%, so hypothesis 4 is not proven. Family shareholders are proven to strengthen the negative relationship between FCF and AU. This result is consistent with the research conducted by Liu et al. (2015).

Family shareholders are generally exposed to agency problems between majority and minority shareholders (Claessens et al., 2012) and they tend to be more concerned with how the company continues to grow and survive than how to increase shareholder value (Anderson and Reeb, 2003 dan Andres, 2008). Minority shareholders do not have the power to make decisions on company policy, thus they cannot prevent the decisions of controlling shareholders who might reduce the value of the company (Solomon, 2017). Older family companies will be more exposed to this managerial entrenchment phenomenon (Andres, 2008). Agency costs can also arise from family involvement in companies with managerial entrenchment. Family controlling shareholders generally maintain

their position in management even though they no longer have enough competencies (Shleifer and Vishny, 1997).

Growing family companies generally run altruistically and interfere with the effectiveness of monitoring so as to increase agency problems. Parents (founders) want to pass on to their children or the next generation who do not necessarily have the competence to run company operations. When the successor does not have the competence in carrying out company operations, they will carry out their duties irresponsibly and even carry out managerial entrenchment, this can occur due to the lack of effectiveness of monitoring (Schulze et al., 2001). In addition, managerial entrenchment can occur due to amoral familism which also tends to occur in family businesses. They tend to have distrust of parties outside the family thereby limiting the process of recruiting human resources from outside parties despite having more adequate competence from family members (Dyer, 2006).

#### ***Control Variable and Asset Utilization***

In Table 4, profitability has a significant positive effect because if the efficiency of a company increases is reflected in high profitability, the company will have a maximum level of asset utilization (Fleming, Heaney, and McCosker, 2005). The size of the company has a significant positive effect. The larger the company will increase asset utilization because the larger companies will reach economies of scale and tend to diversify through synergy between business segments (Singh and Davidson, 2003). Leverage has a positive significant effect on asset utilization. The higher level of monitoring of management in carrying out their duties by creditors will reduce agency costs.

Asset structure shows insignificant influence on asset utilization, indicating that the amount of corporate wealth invested in fixed assets has not been able to influence the level of asset utilization because management has not maximized its use. Company risk has a significant positive

effect. The high risk faced by the company, management will be more careful and efficient in managing assets (Ghazali and Bilal, 2017). The age of the company has a negative influence. The older the company, the fewer investment opportunities that can increase the value of the company, so the possibility of misusing excess cash flows are greater (Gogineni, Linn, and Yadav, 2013).

#### **CONCLUSIONS AND SUGGESTIONS**

In the research on 465 samples of open companies in Indonesia, it is evident that free cash flow (FCF) increases agency costs (reducing asset utilization), which might be due to abuse by opportunist managers who allocate to unprofitable investments aligned with free cash flow hypothesis (Jensen, 1986). Institutional shareholders through effective monitoring and evaluation of management are able to weaken FCF's negative relationship with asset utilization consistent with efficient-monitoring hypothesis (Pound, 1988). However, there is a managerial entrenchment effect because the passivity of shareholders in overseeing management, managerial shareholders strengthen FCF's negative relationship with asset utilization (Simoneti and Gregoric, 2004). Similarly, family shareholders who tend to be altruism and have amoral familism (do not trust outsiders) and do managerial entrenchment even though they do not have the competence that supports, so at the end it reduces the effectiveness of monitoring (Shleifer and Vishny, 1997, Schulze et al. 2001, and Dyer, 2006).

This study has limitations, including: the use of total asset turnover as a proxy for asset utilization has not fully described the investment of productive assets, the relationship between earnings management and asset utilization has not been studied, the use of dummy as a measure of family ownership that can cause research results to be less accurate and consistent, and the research model on managerial ownership only uses linear

regression (not testing non-linear relationships). For further research, it is expected to be able to use more specific asset utilization proxies using productive assets, examine the relationship of asset utilization and earnings management more deeply, to be able to use ratio measurements to measure family ownership and test the position of layers in family company groups such as research by Chandra, Utama, Husodo, and Setia-Atmaja (2017), buying family ownership data access at the Republic of Indonesia Ministry of Law and Human Rights Indonesia (Kemenkumham), and expanded testing of government and foreign ownership structures. Through this research, it is expected to be a reference for companies or controlling shareholders to include institutional ownership of corporate governance and include at least the proportion of managerial ownership above 16% (Simoneti and Gregoric, 2004). Likewise, investors can consider issuers who have institutional ownership as an investment choice.

## REFERENCES

- Ade, Y., (2008). Hubungan Struktur Kepemilikan dan External Monitoring terhadap Agency Cost dan Aliran Kas. *Jurnal Keuangan dan Perbankan*, Vol. 12, No.3 September, hal. 343 – 354.
- Anderson, R.C., and Reeb, D.M. (2003). Founding-family ownership and firm performance: evidence from the S&P 500. *Journal of Finance*, 58, 1301–1328.
- Andres, C. (2008). Large shareholders and firm performance—An empirical examination of founding-family ownership, *Journal of Corporate Finance* 14 (2008) 431–445.
- Ang, J. S., Cole, R. A., and Lin, J. W. (2000). Agency Costs and Ownership Structure. *The Journal of Finance*, 55(1), 81–106. <https://doi.org/10.1111/0022-1082.00201>
- Ayub, M. (2008). Pengaruh Family Control Terhadap Cost Of Debt Pada Perusahaan Yang Terdaftar Di BEI. *Tesis*. Universitas Indonesia
- Bathala, C. T., Moon, K.P., and Rao, R. (1994). Managerial ownership, debt policy and the impact of institutional holdings: An agency perspective. *Financial Management* 23, 38– 50.
- Bhattacharya, U., and Ravikumar, B. (2001). Capital markets and the evolution of family businesses. *Journal of Business* 74, 187–219.
- Brigham, E. F., and Ehrhardt, M. C. (2014). *Financial Management: Theory and Practice*. 14th ed. New York: Thomson South-Western.
- Brown, C., Chen, Y., and Shekhar, C. (2011). Institutional Ownership and Firm Cash Holdings, *SSRN Electronic Journal*.
- Chandra, Y., Utama, C. A., Husodo, Z. A., and Setia-atmaja, L. (2017). Pyramidal Ownership Structure and Cost of Bank Loans: Evidence from Indonesian Business Groups. *Available at SSRN: <https://ssrn.com/abstract=2907583>*
- Claessens, S., Djankov, S., Fan, J., and Lang, L., (1999). Expropriation of Minority Shareholders: Evidence from East Asia. *Policy Research paper 2088*. World Bank, Washington, DC.
- Davis, E.P., 2002. Institutional Investor, Corporate Governance, and The Performance of The Corporate Sector Economic Systems. *Elsevier*, vol. 26(3), pages 203-229, September.
- Davis, J., Donaldson, L. and Schoorman, D. (1997). Towards a Stewardship Theory of Management. *Academy of Management Review*, 22 (1), 20-47.
- Davis, J., Schoorman, R., Mayer, R., and Tan, H. (2000). The trusted general manager and business unit performance. *Strategic Management Journal*, 21, 563–576.

- Dewi, L. C., and Nugrahanti, Y. W. (2014). Pengaruh Struktur Kepemilikan dan Dewan Komisaris Independen Terhadap Nilai Perusahaan (Studi Pada Perusahaan Industri Barang Konsumsi di BEI Tahun 2011–2013), *KINERJA, Volume 18, No.1, Th. 2014: Hal. 64-80*
- Diyah, P. and Widanar, E. (2009). Pengaruh Struktur Kepemilikan Terhadap Nilai Perusahaan: Keputusan Keuangan Sebagai Variabel Intervening. *Jurnal Ekonomi Bisnis dan Akuntansi Ventura*, Vol. 12. No.1, 71-86.
- Ellili, N. O. D. (2012). Managerial entrenchment: Model and impact on the shareholders' wealth. *Corporate Ownership dan Control*, 9(2-4), 449-460.
- Fama, E. and French, K. R., (1992). The Cross Section of Expected Stock Returns. *The Journal of Finance*, 67. 2: 427.
- Ferreira, M. A. and Vilela, A. (2004), Why do firms hold cash? Evidence from EMU countries, *European Financial Management*, 10, 295-319
- Fleming, G., Heaney, R., and McCosker, R. (2005). Agency costs and ownership structure in Australia. *Pacific-Basin Finance Journal*, 13(1), 29–52. <https://doi.org/10.1016/j.pacfin.2004.04.001>
- Fooladi, M., Shukor, Z. A., Saleh, N. M., and Jaffar, R. (2014). The effect of corporate governance and divergence between cash flow and control rights on firm performance: Evidence from Malaysia. *International Journal of Disclosure and Governance*, 11(4), 326–340. <https://doi.org/10.1057/jdg.2013.24>
- Ghazali, A., and Bilal, A. R. (2017). Analyzing the Link Between Agency Problems, Governance and Control Attributes for Pakistan. *E-Finance*, 13(3), 43–65. <https://doi.org/10.1515/eqf-2016-0029>
- Gilson, R. J., and Gordon, J. N. (2003). Controlling Controlling Shareholders, *University of Pennsylvania Law Review*, Vol.152:785.
- Gogineni, S., Linn, S. C. and Yadav, P. K. (2013). Ownership Structure, Management Control and Agency Costs. *Working Paper*. College of Business, University of Wyoming, Laramie WY 82072, USA.
- Hadiprajitno, P. B. (2013). Struktur Kepemilikan, Mekanisme Tata Kelola Perusahaan, dan Biaya Keagenan di Indonesia (Studi Empirik pada Perusahaan di Bursa Efek Indonesia). *Jurnal Akuntansi dan Auditing* Volume 9/No. 2/MEI 2013 : 97-127.
- Howell, D. C. (2007). *Statistical methods for psychology* (6th ed.). Belmont, CA: Thomson Wadsworth.
- Iskandar, T. M., Bukit, R. B., and Sanusi, Z. M. (2012). The moderating effect of ownership structure on the relationship between free cash flow and asset utilisation. *Asian Academy of Management Journal of Accounting and Finance*, 8(1), 69-89.
- Javid, D., Malihi, S. A., and Soheilian, E. (2014). The Impact of Ownership Structure as a Balancing Factor on the Relation between the Free Cash Flow and Optimal Use of the Assets. *Kuwait Chapter of Arabian Journal of Business and Management Review*, 4(1), 407–422. <https://doi.org/10.12816/0018923>
- Jelinek, K., and Stuerke, P. S. (2009). The nonlinear relation between agency costs and managerial equity ownership: Evidence of decreasing benefits of increasing ownership. *International Journal of Managerial Finance*, 5(2), 156–178. <https://doi.org/10.1108/17439130910947886>
- Jensen, M. C. (1993) The modern industrial revolution, exit, and the failure of internal control systems, *Journal of Finance*, 48, 831-880.
- Jensen, M. C., and Meckling, W. H. (1976). Theory of The Firm: Managerial Behavior, Agency Cost and

- Ownership Structure. *Journal of Finance Economics*, 3, 305–360.
- Jensen, M.C. (1986). Agency Cost of Free cash Flow, Corporate Finance, and Takeovers, *American Economic Review*, 76 (2), 323-329.
- Kangarluei, S. J., Motavassel, M., dan Abdollahi, T. (2011). The Investigation and Comparison of Free Cash Flows in The Firms Listed in Tehran Stock Exchange (TSE) with an emphasis on earnings management. *International Journal of Economics and Business Management*, 2(2), 5352-118.
- Khidmat, W. B., and Rehman, M.U. (2014). The Impact of Free Cash Flows and Agency Costs on Firm Performance - an Empirical Analysis of KSE Listed Companies of Pakistan. *Journal of Financial Engineering*, 01(03), 145 - 175.
- Kuan, T.H., Li, C.-S., and Chu, S.H. (2011). Cash holdings and corporate governance in family-controlled firms. *Journal of Business Research*, 64(7), 757–764.  
<https://doi.org/10.1016/j.jbusres.2010.07.004>
- La Porta, R., Lopez-De-Silanes, F., and Shleifer, A. (1999). Corporate Ownership Around the World. *The Journal of Finance*, LIV (2), 471-516. *Literature*, 25(1), 121-132.
- Lawal, M., and Yero, J. (2016). Free Cash Flow, Managerial Ownership and Agency Cost: Evidence from Nigerian Listed Conglomerates. *The 6th Annual Conference of Africa Accounting and Finance Association (AAFA)*.
- Lehn, K. and Poulsen, A., Free Cash Flow and Stock- holder Gains in Going Private Transactions, *Journal of Finance*, Vol. 44, No. 3, pp. 771-787.
- Lin, F.L., and Chang, T. (2008). Does Managerial Ownership Reduce Agency Cost in Taiwan? A Panel Threshold Regression Analysis. *Corporate Ownership and Control*, 5(4).  
<https://doi.org/10.22495/cocv5i4p11>
- Lin, L. and Lin, D. (2014). Agency Cost of Free Cash Flow and Bidders' Long-run Takeover Performance. *Universal Journal of Accounting and Finance*, 2(1), 1-8.
- Lins, K. V. (2003). Equity ownership and firm value in emerging markets, *Journal of Financial Quantitative Analysis* 38, Hal: 159-184
- McClure, B. (2003). *Free Cash Flow: Free, But Not Always Easy*, dikutip dari <http://www.investopedia.org/articels/fundamental/03/091703.asp>
- Morck, R. K., Shleifer, A. and Vishny, R. W. (1998). Management Ownership and Market Valuation: An Empirical Analysis (1998). *Journal of Financial Economics*, Vol. 20, p. 293-315 1998.
- Munawir. (2010). *Analisis Laporan Keuangan*. Edisi 4. Yogyakarta: Liberty
- Murro, P. and Peruzzi, V. (2019). Family Firms and Access to Credit. Is Family Ownership Beneficial?. *Journal of Banking and Finance*, Vol. 101, Hal. 173–187
- Myers, S. C., and Majluf, N. S. (1984). Corporate financing and investment decisions when firms have information that investors do not have. *Journal of Financial Economics*, 13, 187-221
- Nuraina, E. (2012). Pengaruh Kepemilikan Institusional dan Ukuran Perusahaan terhadap Kebijakan Hutang dan Nilai Perusahaan. *Jurnal Bisnis dan Ekonomi (JBE)*, September 2012, Hal 110-125
- Pratiwi, R., and Yulianto, A. (2016). Pengaruh Struktur Kepemilikan dan Komisaris Independen terhadap Biaya Keagenan Perusahaan yang Masuk dalam Indonesia *Most Trusted Companies*, *Management Analysis Journal* 5 (3) (2016)
- PwC. *Family Business Survey 2017: Findings for Indonesia*. PwC Indonesia, 2014.



- Rashid, A. (2015). Managerial Ownership and Agency Cost: Evidence from Bangladesh. *Journal of Business Ethics*, 137(3), 609–621. <https://doi.org/10.1007/s10551-015-2570-z>
- Schulze, W., Lubatkin, M., Dino, R., dan Buchholtz, A. (2001). Agency Relationship in Family Firms: Theory and Evidence. *Organization Science* 12(2): 99-116, Maret 2011.
- Shleifer, A. dan Vishny, R.W. (1997). A survey of corporate governance. *Journal of Finance* 52, 737–783. SEP
- Singh, M., dan Davidson III, W. N. (2003). Agency costs, ownership structure and corporate governance mechanisms. *Journal of Banking dan Finance*, 27(5), 793–816. [https://doi.org/10.1016/S0378-4266\(01\)00260-6](https://doi.org/10.1016/S0378-4266(01)00260-6)
- Solomon, D. (2017). The Voice: The Minority Shareholder’s Perspective. *17 Nevada Law Journal* 739 (2017).
- Stulz, R. (1990). Managerial Discretion and Optimal Financing Policies. *Journal of Financial Economics*, 26, 3-27.
- Syamsudin, L. (2007). *Manajemen Keuangan Perusahaan*. Jakarta: Raja Grafindo Persada.
- Tabachnick, B. G., and Fidell, L. S. (2007). *Using Multivariate Statistics* (5th ed.) Boston: Allyn and Bacon.
- Vidyantie, D. N. and Handayani, R. (2006). The Analysis of The Effect of Debt Policy, Dividend Policy, Institutional Investor, Business Risk, Firm Size, and Earning Volatility to Managerial Ownership Based on Agency Theory Perspective. *Jurnal Bisnis dan Akuntansi*, Vol. 8, No. 2, April, hal. 19-33.
- Wang, G. Y. (2010). The Impacts of Free Cash Flows and Agency Costs on Firm Performance. *Journal of Service Science and Management*, 03(04), 408–418. <https://doi.org/10.4236/jssm.2010.34047>
- Wardhana, L. I., and Tandelilin, E. (2011). Institutional Ownership and Agency Conflict Controlling Mechanism, *Journal of Indonesian Economy and Business*, 18.
- Wardhani, R. and Hendro. (2015). Pengaruh Agency Cost of Free Cash Flow Terhadap Tingkat Konservatisme dan Pengujian Efek Moderasi Kebijakan Hutang, Pendistribusian Kas, Persistensi Kas, dan Tata Kelola Perusahaan, *Jurnal Akuntansi dan Keuangan*, Vol.17, No.1, Mei 2015, 41-56.
- Widanar, E. and Pujiati, D. (2009). Pengaruh Struktur Kepemilikan Terhadap Nilai Perusahaan: Keputusan Keuangan Sebagai Variabel Intervening. *Jurnal Ekonomi Bisnis dan Akuntansi Ventura*, Vol. 12. No.1: Hal.71-86
- Wijayati, F. L. (2015). Analisis Pengaruh Kepemilikan Manajerial, Kepemilikan Institusional, Ukuran Dewan Direksi, Dan Ukuran Dewan Komisaris Terhadap Biaya Keagenan. *EBBANK* Vol. 6, No. 2, Desember 2015 Halaman: 1 – 16.
- Yulianto, A., Kiswanto, Widiyanto, and Yulianto, A. (2014). Linear and Non-linear Approaches in Testing Managerial Ownership on the Firm Value: Evidence Indonesian Firms. *IOSR Journal of Business and Management (IOSR-JBM)* Volume 16, Issue 9.Ver. IV (Sep. 2014), PP 01-05