

Exploring the Reasons Companies Maintain a Stable Dividend Policy Amidst Earnings Fluctuations: A Qualitative Case Study Approach

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Abstract : *This study aims to explore the reasons why companies maintain a stable dividend policy amidst earnings fluctuations using a qualitative case study approach. This phenomenon creates a puzzle in the finance literature because, theoretically, earnings fluctuations should negatively impact dividend stability. Employing an instrumental case study design on three manufacturing companies listed on the Indonesia Stock Exchange, this research interviewed ten key informants, including Finance Directors, CFOs, Financial Managers, and Commissioners, and analyzed secondary documents. Thematic analysis was employed to identify key patterns in the data. The findings generate five main themes, including commitment to signals of stability and predictability, management of shareholder expectations based on investor composition, availability of financial buffers and proactive liquidity management, governance mechanisms and agency control, and strategic considerations of policy flexibility. The results indicate that companies maintain dividend stability through three main strategies: cash reserve policies, access to credit facilities, and accumulation of retained earnings. The theoretical contribution of this research lies in enriching signaling theory and agency theory with perspectives from the emerging market context of Indonesia, as well as providing a mechanistic understanding of dividend smoothing practices.*

Keywords : *Stable Dividend Policy, Earnings Fluctuations, Dividend Smoothing, Qualitative Case Study, Indonesian Emerging Market*

Abstrak : Penelitian ini bertujuan untuk mengeksplorasi alasan perusahaan mempertahankan kebijakan dividen yang stabil di tengah fluktuasi laba dengan menggunakan pendekatan studi kasus kualitatif. Fenomena ini menimbulkan teka-teki dalam literatur keuangan karena secara teoritis fluktuasi laba seharusnya berdampak negatif terhadap stabilitas dividen. Penelitian ini menggunakan desain studi kasus instrumental pada tiga perusahaan manufaktur yang terdaftar di Bursa Efek Indonesia dengan melibatkan sepuluh informan kunci, yaitu Finance Directors, CFO, Financial Managers, dan Commissioners, serta didukung oleh analisis dokumen sekunder. Analisis tematik digunakan untuk mengidentifikasi pola utama dalam data. Hasil penelitian menghasilkan lima tema utama, yaitu komitmen terhadap sinyal stabilitas dan prediktabilitas, pengelolaan ekspektasi pemegang saham berdasarkan komposisi investor, ketersediaan buffer keuangan dan pengelolaan likuiditas secara proaktif, mekanisme tata kelola dan pengendalian agensi, serta pertimbangan strategis terkait fleksibilitas kebijakan. Temuan menunjukkan bahwa perusahaan mempertahankan stabilitas dividen melalui tiga strategi utama, yaitu kebijakan cadangan kas, akses terhadap fasilitas kredit, dan akumulasi laba ditahan. Kontribusi teoretis penelitian ini terletak pada pengayaan signaling theory dan agency theory melalui perspektif pasar berkembang di Indonesia serta memberikan pemahaman mekanistik mengenai praktik dividend smoothing.

Kata Kunci : Kebijakan Dividen Stabil, Fluktuasi Laba, Dividend Smoothing, Studi Kasus Kualitatif, Pasar Berkembang Indonesia

INTRODUCTION

Dividend policy represents one of the most critical financial decisions faced by corporate management, with far-reaching implications for capital market signals, firm value, and shareholder welfare. More than half a century since Lintner's (1956) seminal work, dividend policy continues to

present an unresolved puzzle in modern finance literature. Lintner's classic study, based on in-depth interviews with 28 corporate managers, discovered that firms maintain long-term target payout ratios and tend to adjust dividends gradually in response to earnings changes—a behavior subsequently termed dividend smoothing. The fundamental foundation for understanding stable dividend policy originates from this model, which states that dividend changes are influenced by current earnings and previous dividend levels, with low adjustment speeds indicating strong smoothing behavior. Lintner identified that managers prioritize dividend stability over short-term earnings fluctuations and only adjust dividends when changes in earnings are perceived as permanent.

The intriguing phenomenon at the center of this research is the practice by which firms consistently uphold a stable dividend policy even when their net earnings fluctuate significantly. Theoretically, based on Lintner's (1956) model and predictions from signaling theory (Bhattacharya, 1979; Miller & Rock, 1985), earnings fluctuations should negatively affect dividend stability since dividends are paid from generated earnings. Signaling theory explains that dividends function as a mechanism to convey management's private information regarding future prospects, where stable dividends indicate confidence in long-term performance. Nevertheless, empirical reality reveals firms that continue to pay stable dividends even as their net earnings vary sharply from year to year. This condition also relates to agency theory, which explains that dividend payments can serve as a control mechanism to reduce free cash flow and agency conflicts (Jensen & Meckling, 1976; Jensen, 1986).

This situation raises fundamental questions regarding how management resolves the contradiction between pressures to maintain dividend stability and the operational reality of earnings fluctuations. Brav, Graham, Harvey, and Michaely (2005) confirmed Lintner's findings through a survey of 384 financial executives and in-depth interviews with 23 CFOs in the United States, demonstrating that maintaining dividend levels is a priority equivalent to investment decisions. Management tends to maintain dividend stability unless earnings changes are perceived as permanent, while the relationship between dividends and earnings has weakened alongside the increasing use of share repurchases.

In the context of developing markets, including Indonesia, dividend policy presents unique complexities. Institutional characteristics, concentrated ownership structures, varying levels of investor protection, and regulatory dynamics create a context fundamentally different from developed markets (Jara-Bertin, López-Iturriaga, & Espinosa, 2016). Lifecycle theory further explains that a firm's propensity to pay dividends depends on its stage of development, where mature firms with limited investment opportunities tend to maintain dividend payments, while growing firms prioritize reinvestment (DeAngelo, DeAngelo, & Stulz, 2006). Empirical findings from Latin America show that dividend smoothing is more pronounced in countries with stronger governance mechanisms (Jara-Bertin et al., 2016).

In Indonesia, Singh, Christiana, Upadhyay, Niroula, and Sitanggang (2024) found that stock liquidity significantly affects dividend policy, with information asymmetry acting as a moderating factor. Wirama, Krisnadewi, Artini, and Ardiana (2024) found that capital expenditure negatively affects dividend policy, supporting residual dividend theory. Additional cross-country studies show that dividend policy is influenced by profitability, leverage, ownership structure, and investor perceptions (Visaltanachoti, Luo, & Wei, 2010; Ghodrati, Pourzamani, Nikoumaram, & Banimahd, 2020; Muhozi, 2024). Qualitative evidence also highlights that managerial considerations such as cash flow, firm size, and liquidity play important roles in dividend decisions (William, 2023; Ranny, 2025).

Despite the extensive development of dividend literature, most studies remain dominated by quantitative approaches focusing on financial determinants. These approaches are effective in identifying correlations but limited in capturing managerial decision-making processes. There remains minimal exploration of the reasons behind decisions to maintain stable dividends,

particularly under conditions of earnings volatility, and qualitative studies within the Indonesian context remain scarce.

This study aims to explore the reasons, influencing factors, as well as the decision-making processes and financial management strategies involved in maintaining stable dividend policies amidst earnings fluctuations. The novelty of this research lies in the use of a qualitative case study approach to examine managerial decision-making processes, a specific focus on dividend stability amidst earnings volatility, and the Indonesian context as an emerging market with concentrated ownership structures.

RESEARCH METHOD

This study employs a qualitative approach with an instrumental case study design and an embedded single-case design (Yin, 2018). The selection of a qualitative approach is based on the exploratory nature of the research objective, which aims to achieve an in-depth understanding of the phenomenon from the participants' perspectives (Creswell & Poth, 2018).

The research population consists of companies listed on the Indonesia Stock Exchange meeting the following criteria: (a) consistently paying dividends for at least 5 years; (b) maintaining a stable dividend policy (coefficient of variation of dividends <10%); (c) experiencing significant earnings fluctuations (coefficient of variation of earnings >25%). Purposive sampling using a criterion-based selection strategy (Palinkas et al., 2015) was employed to select three manufacturing companies (food and beverage, pharmaceutical, and state-owned infrastructure). Ten key informants participated, including Finance Directors, CFOs, Financial Managers, Independent Commissioners, and Corporate Secretaries, with 4-20 years of work experience.

Data collection was conducted through semi-structured interviews (duration 60-120 minutes per interview), documentation of financial statements and annual reports for the 2019-2023 period, and passive observation. The primary instrument was the researcher as the human instrument, utilizing an interview guide developed from the theoretical framework.

Trustworthiness was enhanced through source and method triangulation, member checking, prolonged engagement (3 months), peer debriefing, an audit trail, and reflexive journaling (Lincoln & Guba, 1985). Data analysis employed Braun and Clarke's (2006) thematic analysis across six stages: familiarization, coding, theme searching, theme reviewing, theme definition, and report writing.

RESULTS AND DISCUSSION

Company and Participant Profiles

Table 1 presents the dividend policy and earnings fluctuation profiles of the three companies over the 2019-2023 period. Company A (food and beverage, concentrated family ownership >60%) exhibits a DPS coefficient of variation of 6.8% and an earnings coefficient of variation of 30.4%. Company B (pharmaceutical, dispersed ownership with foreign institutions) has a DPS coefficient of variation of 6.1% and an earnings coefficient of variation of 43.2%. Company C (state-owned infrastructure) has a DPS coefficient of variation of 4.9% and an earnings coefficient of variation of 32.8%. All three companies demonstrate high dividend stability despite significant earnings fluctuations, confirming dividend smoothing practices. These findings indicate that dividend decisions are not determined solely by short-term earnings movements, but also by broader strategic considerations related to ownership structure, investor expectations, and corporate reputation.

Table 1. Profile of Dividend Policy and Earnings Fluctuations 2019-2023

Indicator	Company A	Company B	Company C
Coefficient of Variation of DPS	6.8%	6.1%	4.9%
Coefficient of Variation of Earnings	30.4%	43.2%	32.8%
Target Payout Ratio	35-45%	40-50%	25-35%

Thematic Analysis

The thematic analysis generated five main themes.

Theme 1: Commitment to Signals of Stability and Predictability

All participants (10/10, 100%) stated that maintaining stable dividends is a top priority. The Finance Director of Company A (P-A1) stated: "We are very cautious when deciding on dividend changes because the market reads every change as a signal. If we cut dividends when earnings have only temporarily declined, investors will assume there is a fundamental problem." The CFO of Company B (P-B1) added: "We have built a reputation as a predictable company. Institutional investors such as pension funds and mutual funds require certainty of cash flow from dividends."

Theme 2: Management of Shareholder Expectations

Shareholder composition influences the level of commitment to dividend stability. The Financial Planning Manager of Company C (P-C2) explained: "As a state-owned enterprise, we have the government as our primary shareholder, which expects dividends as a source of non-tax state revenue. This expectation is very strong." Conversely, the Corporate Secretary of Company B (P-B3) stated: "We routinely conduct investor outreach to manage expectations. With good communication, investors understand why dividends need not fluctuate in line with earnings."

Theme 3: Availability of Financial Buffers

The study identified three financial buffer strategies. The Financial Manager of Company A (P-A2) explained the cash reserve policy: "We have an informal policy of maintaining a cash balance equivalent to at least 2-3 months of annual dividend requirements." The CFO of Company B (P-B1) explained credit access: "We have a committed credit facility from partner banks that can be drawn at any time." The Finance Director of Company C (P-C1) explained the use of retained earnings: "We have built up substantial accumulated retained earnings from previous years when earnings were high."

Theme 4: Governance Mechanisms and Agency Control

The Independent Commissioner of Company A (P-A3) explained the alignment of interest: "The controlling owners (founding family) have a clear preference for regular dividends because dividends are a source of personal income. There is a strong alignment of interest between owners and management." The Head of Treasury Division of Company B (P-B2) stated: "Because ownership is dispersed, dividend stability serves as a reputation device. Investors know that the commitment to stable dividends remains strong even when earnings are volatile."

Theme 5: Policy Flexibility

A member of the Board of Commissioners of Company C (P-C3) explained: "We have a clear dividend policy framework. We commit to a certain payout ratio range, rather than an absolute dividend amount. Smoothing is done wisely." The Finance Director of Company A (P-A1) added: "We communicate our target payout ratio policy of 35-45% of consolidated earnings. This provides room to maneuver."

Discussion

Relevance of Signaling Theory in the Indonesian Context

Finding that commitment to stability signals serves as the primary motivation confirms the relevance of signaling theory in the Indonesian capital market. Brav et al. (2005), in their survey of 384 U.S. CFOs, similarly found that maintaining dividend levels is a priority equivalent to investment decisions. However, this study reveals an important nuance: the signal intended to be transmitted is not merely "the company is healthy" but rather "the company is predictable." Predictability is highly valued by institutional investors (pension funds, mutual funds, insurance companies) that require regular cash flow.

This finding aligns with Al-Najjar and Kilincarslan (2017) in Turkey, showing that firms in emerging markets adopt stable dividend policies as a signaling mechanism. The Indonesian

companies studied demonstrate high levels of dividend stability (DPS coefficient of variation <7%), indicating sophisticated dividend smoothing practices. Further research by Michaely, Rossi, and Weber (2021) indicates that firms with higher earnings quality tend to have more stable dividend policies, confirming that stable dividends serve as a credible signal of earnings quality. In the Indonesian context, this finding reinforces the argument that management uses dividend stability as a mechanism to differentiate themselves from other firms whose earnings may be more volatile but are not accompanied by strong dividend commitments.

The findings indicate that dividend stability serves as a mechanism to reduce information asymmetry in an environment with limited regulatory enforcement. Unlike developed markets where stringent disclosure requirements mitigate information gaps, Indonesian capital markets exhibit varying degrees of transparency. Consequently, management utilizes stable dividends as a credible substitute for formal disclosures. This echoes the argument by Singh et al. (2024) that information asymmetry moderates the relationship between stock liquidity and dividend policy. By maintaining dividend predictability, firms effectively lower the information barrier that external investors face when evaluating corporate performance.

The study reveals that the credibility of dividend signals depends heavily on the firm's historical consistency. As noted by the finance director of Company A, a single dividend cut can erase years of accumulated trust, regardless of the underlying reasons. This finding supports the costly signaling framework proposed by John and Williams (1985), where only firms with genuinely sustainable earnings can afford to uphold stable payouts over extended periods. Firms with volatile earnings but insufficient cash buffers would eventually be forced to reduce dividends, exposing their lack of fundamental strength.

The preference for predictability over absolute dividend growth distinguishes emerging market behavior from that of developed markets. While Brav et al. (2005) found that U.S. CFOs prioritize maintaining dividends as equivalent to investment decisions, the Indonesian context adds another layer: institutional investors such as pension funds and mutual funds value predictable cash flows more than potential capital gains. This preference arises from the relative underdevelopment of fixed-income markets in Indonesia, forcing income-seeking investors to rely on dividend-paying equities as substitutes for bonds.

Furthermore, this study reveals that the effectiveness of signaling theory in explaining stable dividend policy in Indonesia depends greatly on management's credibility in the eyes of the market. As expressed by P-A1 (Finance Director of Company A), signals transmitted through stable dividends will only be trusted by the market if the firm has a consistent track record of meeting its dividend commitments. This finding aligns with the argument by John and Williams (1985) that dividends constitute a costly signal because firms without good prospects would be unable to maintain stable dividend payments over the long term. Thus, stable dividend policy functions as a screening device that separates high-quality firms from low-quality firms in the Indonesian capital market, which remains dominated by high information asymmetry (Singh et al., 2024).

The signaling function of stable dividends operates differently across shareholder compositions. In companies with concentrated family ownership (Company A), signals are directed primarily at minority investors and creditors who lack access to internal information. In contrast, for state-owned enterprises (Company C), stable dividends signal fiscal reliability to government principals and the broader public. This differentiated signaling strategy has not been extensively documented in prior literature, which tends to treat signaling as a uniform process regardless of ownership structure.

The Role of Governance and Ownership Structure

The observation that ownership structure exerts an influence on stable dividend policy is consistent with the findings of Jara-Bertin et al. (2016) in Latin America, wherein nations with robust governance frameworks exhibit a slower speed of dividend adjustment. Nevertheless, the current investigation contributes an additional perspective: within enterprises characterized by

concentrated ownership—specifically Companies A and C—dividend stability proves to be more pronounced as a consequence of interest alignment.

This result enhances agency theory as articulated by Jensen (1986). In contrast to traditional expectations that concentrated ownership engenders conflicts between majority and minority shareholders, the Indonesian context of stable dividend policy reveals that controlling proprietors actually emerge as principal advocates of stability, driven by their direct stake in consistent dividend cash flows. This observation lends support to the outcome model proposed by La Porta et al. (2000). Furthermore, research conducted by Wirama et al. (2024) in Indonesia determined that capital expenditure exerts a negative influence on dividend policy, thereby corroborating the residual dividend theory hypothesis that firms prioritize investment financing prior to distributing dividends.

Beyond ownership structure, the present study further identifies the significant role played by independent boards of commissioners in mediating the relationship between controlling owners and management concerning stable dividend policy. Participant P-A3, serving as the Independent Commissioner of Company A, disclosed that the independent board of commissioners acts as a balancing safeguard, mediating between the preference of controlling owners for substantial dividends and the organization's requirement to preserve adequate liquidity. This finding is consistent with the work of Ranny (2025) in Indonesia, which demonstrated that good corporate governance (GCG) exerts a statistically significant positive effect on dividend policy ($p = 0.0194$). Stated differently, effective corporate governance not only promotes dividend distributions in general but also fosters dividend stability by ensuring that dividend determinations rest upon rational business considerations rather than being driven exclusively by pressure from controlling owners.

The presence of independent commissioners serves to mediate the inherent tension between the dividend demands of controlling owners and the liquidity requirements of the firm. As expressed by the independent commissioner of Company A, the board functions as a balancing instrument that prevents majority shareholders from extracting excessive dividends at the expense of long-term financial viability. This finding extends the outcome model of La Porta et al. (2000) by identifying the precise governance mechanism—independent boards—through which shareholder protection is operationalized within concentrated ownership environments.

The alignment of interests between controlling owners and management within family-owned enterprises paradoxically reinforces dividend stability rather than disadvantaging minority shareholders. Traditional agency theory posits that controlling owners expropriate minority interests by reducing dividend payouts (Jensen & Meckling, 1976). However, in the three Indonesian firms examined, families depend on regular dividends as a source of personal income, thereby generating a powerful incentive to sustain stable distributions. This alignment proves beneficial for minority shareholders as well, given that they receive predictable cash flows without requiring active monitoring of management.

Governance mechanisms in state-owned enterprises diverge fundamentally from those in private firms owing to political economy considerations. For Company C, dividend stability constitutes not merely a financial decision but rather a political commitment to the state budget. The government, acting as the majority shareholder, anticipates dividends as a source of non-tax revenue, thereby creating a form of "political dividend smoothing." This phenomenon has received limited attention in mainstream agency literature, which typically assumes profit maximization as the sole objective. Future research ought to investigate how political incentives shape dividend policies in state-controlled enterprises across emerging economies.

The effectiveness of governance mechanisms in promoting dividend stability is contingent upon the enforcement capacity of the legal environment. Although Indonesia has adopted corporate governance codes comparable to those in developed markets, enforcement remains inconsistent. Consequently, internal mechanisms—such as independent commissioners and audit committees—

carry greater weight than external legal protections. This observation aligns with the findings of Jara-Bertin et al. (2016), who reported that dividend smoothing is more intense in countries with superior governance scores. However, the present study adds that board independence compensates for weaker judicial enforcement

Practical Mechanisms of Dividend Smoothing

The present investigation identified three operational mechanisms employed by firms to sustain dividend stability: the maintenance of cash reserves, access to committed credit facilities, and the strategic accumulation of retained earnings. These results are consistent with the findings of Leary and Michaely (2011), who demonstrated that firms experiencing elevated earnings volatility tend to adopt more pronounced dividend smoothing practices and concurrently hold larger cash buffers. Furthermore, Visaltanachoti, Luo, and Wei (2010) observed that firms which persist in distributing dividends are generally characterized by more substantial cash reserves.

The cash reserve strategy documented in this research bears resemblance to the liquidity management behaviors reported by Tandelilin (2015) within the Indonesian setting. That study revealed that Indonesian firms operating between 1994 and 1999 exhibited a tendency to adjust dividend payments gradually toward their target levels, with an adjustment speed of approximately 0.36, thereby indicating robust dividend smoothing behavior facilitated by the accumulation of cash reserves. One informant, the Head of the Treasury Division of Company B (P-B2), highlighted that the presence of a committed credit facility affords management psychological reassurance to continue dividend distributions even during periods of constrained cash flow, grounded in the confidence that banking partners will supply necessary liquidity when required.

The observation concerning the utilization of accumulated retained earnings as a dividend smoothing mechanism introduces novel insights into the interconnection between dividend policy and earnings management. As articulated by the Finance Director of Company C (P-C1), the organization deliberately refrains from distributing its entire net income during periods of high profitability, instead allocating a portion to retained earnings for subsequent use when earnings diminish. This practice effectively moderates the variability of dividends distributed to shareholders. Importantly, in contrast to earnings management techniques frequently associated with the manipulation of accounting figures (Schipper, 1989), dividend smoothing achieved via retained earnings accumulation constitutes a transparent and auditable practice, given that such allocations are explicitly disclosed in financial statements. This evidence reinforces the proposition that dividend smoothing does not represent a form of financial manipulation but rather constitutes a prudent approach to corporate financial management. This perspective aligns with Lintner's (1956) classic observation that rational financial managers retain earnings during favorable periods to secure the continuity of dividend disbursements during unfavorable ones.

The cash reserve strategy identified in this study functions as a self-insurance mechanism against earnings volatility. Unlike formal credit lines, which necessitate negotiation and impose interest expenses, cash reserves provide immediate and unconditional liquidity. The financial manager of Company A described the practice of maintaining cash balances equivalent to two to three months of annual dividend obligations, thereby effectively converting a volatile earnings stream into a stable dividend stream. This approach echoes the precautionary savings motive documented by Leary and Michaely (2011), while extending their work by specifying the reserve levels required to achieve dividend smoothing.

Second, committed credit facilities serve as a complementary buffer that mitigates the opportunity cost associated with holding excessive cash reserves. Whereas cash reserves remain idle and generate modest returns, credit lines incur fees only upon actual drawdown. The Chief Financial Officer of Company B (P-B1) emphasized that access to bank facilities provides psychological comfort, enabling management to commit to stable dividends without resorting to the hoarding of excessive cash. This hybrid strategy—combining cash reserves to absorb normal

fluctuations and credit lines to address severe downturns—represents a sophisticated liquidity management approach that has not been extensively detailed in prior dividend smoothing literature.

The accumulation of retained earnings during periods of high profitability constitutes a form of intertemporal redistribution that circumvents the adverse signal associated with dividend reductions. Rather than distributing all profits when earnings are elevated, firms set aside a portion within retained earnings to supplement dividend payments during periods of earnings decline. As explained by the finance director of Company C (P-C1), this practice remains transparent and subject to external audit, thereby distinguishing it from earnings management achieved through accounting manipulation (Schipper, 1989). This finding provides empirical support for Lintner's (1956) original insight that rational managers smooth dividends by conserving profits in prosperous years to sustain payouts in less prosperous ones.

The adoption of target payout ratio ranges in place of fixed absolute dividend amounts affords the operational flexibility necessary for sustainable smoothing. All three companies explicitly communicated target ranges—for example, 35% to 45% of consolidated earnings—rather than committing to a specific dividend per share. This framework permits management to adjust the actual payout ratio within the prescribed range in response to realized earnings, while preserving the appearance of stability. This tactical nuance has been largely overlooked in quantitative studies, which typically model dividend smoothing as a mechanical partial adjustment process without accounting for managerial discretion within policy bands.

Theoretical Implications

This research provides several theoretical contributions: (1) enriching signaling theory by demonstrating that in emerging market contexts, the signal of predictability is as important as the signal of corporate health; (2) extending agency theory by showing that concentrated ownership can serve as a driver of dividend stability rather than merely a source of conflict; (3) providing a mechanistic understanding of how dividend smoothing is operationally implemented.

CONCLUSION

This study concludes that companies maintain stable dividend policies amidst earnings fluctuations for three primary reasons: commitment to signals of stability and predictability, management of shareholder expectations based on investor composition, and the availability of financial buffers. Influencing factors include internal factors (profitability, retained earnings, cash reserves), external factors (investor expectations, market pressures), and agency factors (ownership structure, alignment of interest). Financial management strategies encompass cash reserve policies, access to credit facilities, and accumulation of retained earnings, supported by flexible dividend policy frameworks in the form of target payout ratio ranges.

Limitations of this study include limited generalizability (only three manufacturing companies), potential retrospective bias, and restricted access to internal documents. Future research could expand sectoral coverage, employ mixed methods, or conduct longitudinal studies.

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