# Impact of Corporate Governance Practices on Cash Holdings: A Study on Largest Market Capitalization Companies Listed in Sri Lanka

Farveen, M.N.M*

*Department of Business Finance, University of Peradeniya, Sri Lanka*

**Abstract**

Various corporate finance theories propose conflicting views on the link between corporate governance and cash holdings. This study examines the role of corporate governance in managing cash holdings, focusing on the largest companies by market capitalisation listed on the Colombo Stock Exchange (CSE) from 2021 to 2025. Using multiple regression analysis on annual report data from 100 firms, it evaluates the influence of board structure, measured by board size, independence, and meeting frequency and ownership structure, encompassing institutional and managerial ownership, on cash holdings. The findings reveal that institutional ownership positively impacts cash holdings, while managerial ownership and board independence significantly reduce them. Board size and meeting frequency showed no notable effect. Among control variables, firm size negatively influences cash holdings, leverage has a positive effect, and growth exhibits no significant relationship. This research provides valuable insights for financial managers, investors, and stakeholders, highlighting key factors influencing corporate cash reserves.

***Keywords*:** corporate governance, return on equity, return on assets, cash holdings

## 1. Introduction

The relationship between corporate governance practices (CGPs) and a corporate cash holding has gained significant attention due to its implications for company performance and shareholder value. Corporate governance, which comprises systems and processes that ensure a firm's accountability and transparency, plays a critical role in managing conflicts of interest between shareholders and managers. These conflicts, often explained through agency theory, arise when managers prioritise personal interests over optimal resource allocation. For instance, weak governance structures may lead to excessive cash holdings, allowing managers to misuse funds through unproductive investments or costly acquisitions, ultimately harming shareholder wealth (Jensen, 1986; Dittmar, Mahrt-Smith & Servaes, 2003). Strong governance mechanisms, such as oversight, independence, and regular meetings, help monitor managerial decisions and align them with shareholder interests, ensuring cash reserves are utilised strategically to maximise firm value.

* Corresponding author: nashathfarwin911@gmail.com

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Corporate activities rely heavily on cash holdings, as cash serves as a vital resource for driving operational, investment, and financing functions (Hassanein & Kokel, 2019). Companies must carefully decide whether to utilise available cash or retain it to address liquidity requirements, investment opportunities, or operational needs. Akhtar et al. (2018) identify two key reasons why companies hold substantial cash reserves. Firstly, holding large amounts of cash provides flexibility for internal financing, particularly when companies need funds but aim to avoid liquidating non-cash assets or incurring high costs associated with external financing. Secondly, cash reserves act as a safeguard, enabling companies to mitigate risks and prepare for potential poor investment decisions.

The primary goal of a company's operations is to enhance shareholder value while meeting stakeholder obligations. Effective corporate governance plays a critical role in ensuring that management operates the business in alignment with stakeholder interests. Strong corporate governance functions as a monitoring mechanism that reduces management's focus on personal gains and minimizes agency problems between managers and shareholders. In contrast, weak corporate governance allows management to prioritize their interests, such as holding excessive cash reserves (Ajanthan & Kumara, 2017).

The importance of corporate governance has become a focal point for both business leaders and regulators globally, especially in the aftermath of the global financial crisis. The crisis highlighted numerous failures in corporate governance, prompting international regulators to implement stricter regulatory controls. Consequently, effective corporate governance plays a critical role in society at large. It promotes the efficient utilisation of limited resources within organisations and across the economy, ensures that resources are directed toward the most productive sectors or entities, helps managers maintain their focus on enhancing organisational performance, serves as a mechanism for selecting the most capable executives to manage scarce resources effectively, and it compels organisations to adhere to societal rules, regulations, and expectations.

Empirical studies have highlighted the importance of specific governance attributes in managing cash holdings. For example, Opler et al. (1999) found that firms with high cash flow risks and better investment opportunities tend to hold more cash as a precautionary measure. However, inefficient governance can exacerbate free cash flow problems, encouraging managers to hoard excess cash unnecessarily. This study focuses on the largest market capitalisation companies in Sri Lanka, excluding the banking and financial sector, from 2021 to 2025. It examines governance variables such as ownership structure, board size, board independence, and board meetings to determine their influence on cash management practices. By analysing these factors, the study aims to provide empirical evidence on how robust governance frameworks can optimise cash holdings, balancing liquidity needs with shareholder value creation in an evolving economic environment.

Corporate cash holdings provide firms with liquidity to meet operational needs, finance investment opportunities, and withstand financial uncertainty. However, excessive cash accumulation can create agency problems when managers have considerable discretion over corporate resources. Therefore, effective corporate governance is expected to influence how firms balance liquidity needs against the potential costs of holding excess cash.

Despite the theoretical importance of this relationship, empirical evidence remains inconclusive, particularly across emerging markets. Recent studies demonstrate that the influence of corporate governance on cash holdings varies according to institutional and firm-specific characteristics. Jiang et al. (2024), for example, found that several board characteristics had insignificant effects on cash holdings, while block ownership reduced cash holdings among manufacturing firms in Pakistan. Similarly, recent evidence from Asian markets suggests that stronger governance mechanisms can reduce corporate cash accumulation, although the magnitude of these effects varies across institutional environments. These findings indicate that the governance–cash holding relationship cannot necessarily be generalised across different emerging markets.

In Sri Lanka, the existing evidence is also relatively limited and largely based on earlier periods. Ajanthan and Kumara (2017) examined 90 listed companies and reported that board size and gender diversity negatively influenced cash holdings, while Kengatharan (2017), using 26 listed manufacturing firms during 2011–2015, found mixed effects among different governance mechanisms. Although these studies provide an important foundation, their earlier observation periods and different sample characteristics may not adequately capture the current corporate governance and liquidity environment of Sri Lankan listed firms.

Accordingly, the key research problem is the limited recent evidence on whether corporate governance mechanisms continue to influence corporate cash-holding decisions among leading Sri Lankan listed companies. There is insufficient evidence examining ownership-based mechanisms together with board-level governance mechanisms within a contemporary Sri Lankan setting. This study addresses this gap by examining the effects of managerial ownership, institutional ownership, board independence, board meetings, and board size on cash holdings among the largest market-capitalisation non-financial companies listed on the Colombo Stock Exchange during 2021–2025. By providing recent evidence from Sri Lanka, the study extends the emerging-market literature and offers a contemporary assessment of whether corporate governance mechanisms constrain or encourage corporate cash accumulation.

## 2. Literature Review

### 2.1 Theoretical review

Keynesian Theory provides an early foundation for understanding why firms hold cash. Keynes (1936) identified transaction and precautionary motives for holding liquid resources, suggesting that firms maintain cash to meet routine obligations and protect themselves against unexpected financial needs. From a corporate perspective, the level of cash required depends on the firm's operational conditions, investment opportunities and uncertainty. Corporate governance mechanisms can influence how these liquidity requirements are assessed and managed. Board size may provide broader expertise for evaluating liquidity needs, while board independence can enhance objective oversight of cash-management decisions. Similarly, an effective audit committee can strengthen financial monitoring and ensure that cash reserves are maintained for legitimate corporate purposes. Institutional ownership may encourage disciplined liquidity management through stronger external

monitoring, whereas CEO duality may increase managerial discretion in determining the level of precautionary cash. Therefore, Keynesian Theory explains the fundamental motives for holding cash, while governance mechanisms influence the effectiveness with which those motives are translated into corporate cash-holding decisions.

Agency Theory provides the principal theoretical foundation for explaining the relationship between corporate governance and cash holdings. Jensen and Meckling (1976) argue that the separation of ownership and control can create conflicts between shareholders and managers because managers may pursue objectives that do not fully correspond with shareholders' interests. This issue is particularly relevant to cash holdings because cash represents a highly liquid and discretionary corporate resource. Managers may retain excessive cash instead of distributing it to shareholders or investing it in value-enhancing opportunities, thereby creating agency costs (Jensen, 1986). In this context, board size can influence the monitoring capacity and effectiveness of the board, while board independence can strengthen managerial oversight by reducing the influence of executive directors. CEO duality is one individual simultaneously serves as both CEO and board chair, may increase managerial power and weaken board monitoring. An effective audit committee can improve financial reporting oversight and internal control, reducing opportunities for inappropriate cash accumulation. In addition, institutional ownership can provide strong external monitoring because institutional investors generally possess greater expertise and incentives to influence managerial decisions. Consequently, Agency Theory suggests that the effectiveness of these five governance mechanisms can determine the extent to which managers retain, utilise or accumulate corporate cash (Harford et al., 2008).

Financing Hierarchy Theory, also known as the Pecking Order Theory, provides another explanation for corporate cash holdings by focusing on firms' financing preferences. Myers and Majluf (1984) argue that information asymmetry between managers and external investors causes firms to prefer internal financing over external financing, followed by debt and, as a last resort, equity financing. Accordingly, firms may retain cash generated from operations as an internally available source of finance for future investment and operating requirements. The five governance mechanisms can influence this financing decision by affecting managerial discipline, financial planning and resource allocation. Board size and board independence may enhance the quality of financing and investment decisions, while the audit committee can improve the reliability of financial information used in those decisions. Institutional ownership may encourage managers to utilize retained cash efficiently rather than accumulating unnecessary reserves. Conversely, CEO duality may affect the extent of managerial discretion over the retention and use of internally generated funds. Thus, Financing Hierarchy Theory establishes a connection between governance mechanisms and cash holdings by explaining how firms' preference for internal financing can influence their decision to retain liquid resources.

Trade-Off Theory provides a direct explanation of firms' decisions regarding the optimal level of cash holdings. The theory proposes that firms balance the benefits of holding cash against the costs associated with maintaining excessive liquidity. Cash provides several benefits, including financial flexibility, the ability to meet unexpected obligations, reduced

dependence on costly external financing and the capacity to undertake profitable investment opportunities when they arise. However, holding excessive cash can generate opportunity costs and increase managerial agency problems (Opler et al., 1999). Corporate governance can therefore play an important role in determining whether a firm's cash balance remains within an economically appropriate range. Board size and board independence can enhance oversight of liquidity decisions, while the audit committee can strengthen financial control. Institutional ownership can encourage managers to avoid inefficient accumulation of cash, whereas CEO duality may increase managerial discretion and potentially affect the firm's preferred cash level. Therefore, Trade-Off Theory suggests that effective governance mechanisms can help firms balance the benefits of liquidity with the costs associated with excessive cash holdings.

Taken together, these four theories provide complementary explanations for the relationship between corporate governance and corporate cash holdings. Keynesian Theory explains the transaction and precautionary motives underlying firms' demand for cash; Agency Theory explains how governance mechanisms can constrain managerial discretion and reduce the inefficient accumulation of cash; Financing Hierarchy Theory explains the importance of cash as an internally generated financing source; and Trade-Off Theory explains how firms balance the benefits and costs of liquidity to determine an appropriate level of cash holdings. Accordingly, board size, board independence, CEO duality, audit committee, and institutional ownership can influence corporate cash holdings through their effects on managerial monitoring, decision-making authority, financial control, financing preferences and resource allocation. This integrated theoretical framework therefore provides a stronger basis for examining how corporate governance mechanisms shape firms' cash-holding policies, particularly in emerging-market contexts where governance structures may play a significant role in mitigating agency problems and improving financial decision-making (Harford et al., 2008; Kengatharan, 2017).

### 2.2 Empirical review and hypotheses

In an ideal market with no transaction costs or information asymmetry, companies wouldn't need to accumulate cash reserves, as external funds could be raised effortlessly. However, in the real world, market imperfections such as transaction costs and information asymmetry drive firms to hold cash for precautionary, transactional, and speculative motives. Early studies, including those by Opler et al. (1999) and Keynes (1936), highlight these motives, while further research, such as by Jensen (1986), suggests that firms with high cash holdings may face agency problems if managers misuse the funds. Corporate governance plays a crucial role in mitigating these issues, as strong governance mechanisms can prevent managers from squandering cash on low-return projects. Research by Dittmar et al. (2003) and others indicates that firms in countries with weak investor protection tend to hold more cash, reflecting agency problems, while strong governance reduces these issues. Studies on the effect of firm-level governance, such as those by Harford et al. (2008) and Chen (2008), suggest that effective governance structures can limit cash misuse, enhancing firm value. However, inconsistent findings across different countries and contexts, such as those by Bokpin et al. (2011) and Talbi and Menchaogi (2023), show that the relationship between

corporate governance and cash holdings is complex, with factors like board size, CEO duality, and managerial ownership significantly influencing cash reserves in various markets.

Managerial ownership (MO) refers to the percentage of a firm's equity owned by its executive directors. Research suggests that the relationship between managerial ownership and cash holdings (CH) is complex. Some studies, like those by Kalcheva and Lins (2007) and Mohd et al. (2015), indicate a positive relationship, where managers accumulate cash to reduce financial risk and increase decision-making flexibility. However, according to Jensen (1986), high cash reserves may reflect managers' personal agendas rather than shareholder interests, leading to potential conflicts. Agency theory suggests that greater managerial ownership aligns managers' interests with shareholders, reducing agency costs and leading to lower cash holdings (Talbi & Menchaoui, 2023). On the other hand, at high ownership levels, the entrenchment effect might cause managers to retain more cash for personal gain (Marck, Shleifer, & Vishny, 1988). Therefore, this study hypothesises a negative relationship between managerial ownership and cash holdings, where higher ownership reduces cash reserves due to the alignment of managerial and shareholder interests.

*$H_1$: There is a negative significant relationship between Managerial ownership and cash holdings*

Institutional ownership (IO) refers to the shares held by large investors such as banks, insurance companies, and investment firms. Institutional investors are known to monitor management, enhance capital allocation, and improve corporate governance (Luong et al., 2017). This oversight helps align management's actions with shareholder interests, reducing agency problems (Hesty, 2019). While some studies, like those by Shery Yuliana and Ketut (2016), suggest no effect of IO on cash holdings, others argue that institutional ownership encourages transparency and effective cash management, leading to optimal cash holding levels (Hesti Anita, 2019; Masood & Shah, 2014). Furthermore, research by Mawardi and Nurhalis (2018) indicates that institutional ownership positively impacts cash holdings by improving supervision. Based on these findings, the study hypothesises a positive and significant relationship between institutional ownership and cash holdings.

*$H_2$: There is a positive significant relationship between institutional ownership and cash holdings.*

Board independence (BIND) enhances the oversight of management, ensuring that they act in the best interests of shareholders. Agency theory suggests that independent directors can reduce agency costs by protecting minority shareholders and minimising managerial opportunism (Chahine & Filatotchev, 2008; Kim et al., 2007). Independent boards improve information disclosure, reduce information asymmetry, and provide stronger oversight, thus discouraging managers from accumulating excessive cash for personal gain (Lee & Lee, 2009; Opler et al., 1999). While some studies, like those by Opler et al. (1999), suggest a positive relationship between BIND and cash holdings due to enhanced shareholder protection, others, such as Ozkan and Ozkan (2004), argue that lower information asymmetry may reduce the need for large cash reserves, leading to a negative relationship. Empirical evidence, however, largely supports the view that independent boards help reduce corporate

cash reserves by improving managerial accountability (Hassanein & Kokel, 2019; Abuhijleh & Zaid, 2023). Based on this, the study hypothesises a negative significant relationship between board independence and cash holdings.

*$H_3$: There is a negative significant relationship between board independence and cash holdings.*

Board meetings (BM) provide a platform for board members to oversee management and ensure alignment with shareholders' interests. Agency theory suggests that frequent meetings can enhance oversight by improving monitoring of financial reporting and preventing opportunistic behaviour (Alshirah et al., 2000; Vafeas, 1999). Studies by Aldamen et al. (2012) and Zhang et al. (2007) support the idea that frequent meetings improve board effectiveness and internal control. However, some argue that excessive meetings may impose costs, such as management time and reduced time for directors to engage independently (Vafeas, 1999; Jensen, 1993). Despite this, research by Abuhijleh and Zaid (2022) shows that increased board meetings lead to a significant decrease in cash holdings, suggesting that more frequent meetings contribute to better cash management. Therefore, the hypothesis predicts a significant negative relationship between board meetings and cash holdings.

*$H_4$: There is a negative significant relationship between board meetings and cash holdings*

Board size (BS) influences the effectiveness of company management. Larger boards are often associated with greater diversity in expertise, which can enhance decision-making and provide valuable advice to management (Cheng et al., 2008; Zahra & Pearce, 1989). Studies suggest that larger boards reduce the discretionary power of managers, improving governance and firm reputation (Musteen et al., 2010). However, excessively large boards can lead to inefficiencies, such as poor communication, slow decision-making, and coordination issues, which may result in weaker monitoring and allow managers to accumulate excessive cash reserves for personal gain (Said et al., 2009; Boubaker & Nguyen, 2015). Research by Al-Dhamari & Ismail (2014) and Abuhijleh & Zaid (2023) supports the idea that larger boards can negatively impact cash holdings, as ineffective oversight allows managers to retain more cash. Thus, the hypothesis suggests a significant negative relationship between board size and cash holdings.

*$H_5$: There is a significant negative relationship between board size and cash holding*

## 3. Methods

The cash holdings denotes cash and cash equivalents divided by total assets, while the independent variable of this study is corporate governance practices, which include managerial ownership, institutional ownership, board independence, board meetings, and board size. Managerial ownership refers to the portion of shares held by the management team, enabling them to influence company strategies as both managers and shareholders (Khan et al., 2013). Institutional ownership represents shares held by large financial institutions like mutual funds, banks, and insurance companies, reflecting their stake in corporate governance (Investopedia, 2023). Board independence highlights the role of non-

executive directors, ensuring impartial decision-making free from conflicts of interest. Board meetings serve as official gatherings where directors assess performance, discuss policies, and address key issues, with formal minutes providing a legal record. Finally, board size refers to the number of directors overseeing company operations. While larger boards offer diverse perspectives and external connections, excessively large boards may lead to inefficiencies and reduced management involvement (Abeysekera, 2010; Hermalin & Weisbach, 2003).

**Table 1: Definitions of variables**

| Variable | Symbol | Measurement |
|---|---|---|
| Cash holdings | CH | Cash and cash equivalents divided by total assets |
| Managerial ownership | MO | Shares owned directly by directors, supervisors & top management / total number of outstanding shares |
| Institutional ownership | IO | shares owned by institutions / total number of outstanding shares |
| Board independence | BI | independent directors divided by the total number of directors |
| Board Size | BS | Total number of members of the board of directors |
| Board Meeting | BM | Total number of Board Meetings in a year |
| Firm Size | FS | Natural Logarithm of total assets |
| Leverage | LEV | Total debt / total assets |
| Growth | GR | $\text{Sales}_{t} - \text{sales}_{t-1} / \text{Sales}_{t-1}$ |

In this study, firm size, growth and leverage are used as control variables. Firm size is measured by the natural logarithm of total assets at the firm level. As discussed in Dixon, Guariglia, and Vijayakumaran (2017). Larger companies typically have more resources to generate profits and can potentially accumulate more cash. Leverage, which is defined as the total debt-to-total-assets ratio, is used to capture the effect of capital structure. Companies with higher levels of leverage often need to keep more cash on hand to maintain their liquidity, that is, to manage their loan repayments and interest.

To assess the impact of corporate governance on cash holdings, fixed effects regression models are utilised as they effectively address firm-specific characteristics. In contrast, pooled Ordinary Least Squares (OLS) fails to account for potential endogeneity issues arising from unobserved heterogeneity, such as differences in managerial competency. To determine whether the fixed effects model (FEM) or the random effects model (REM) is more appropriate for the dataset, the Hausman specification test is conducted. The test produces highly significant results, with a chi-squared statistic of and a p-value of 0.000, highlighting substantial differences in the coefficients between the two models. This indicates the presence of significant firm-specific effects and their association with the dependent variable. Therefore, the FEM is deemed the more reliable and suitable framework for accurately capturing the relationship between corporate governance and cash holdings in this analysis.

The population of the study comprises 284 companies listed on the Colombo Stock Exchange (CSE), representing 20 GICS industry groups. From this population, a sample of 100 companies is selected based on market capitalisation, focusing on the largest and economically significant firms in the Sri Lankan capital market. The sample covers major sectors, including Food, Beverage & Tobacco, Capital Goods, Materials, Consumer Services, Retailing, Healthcare, Energy, Consumer Durables & Apparel, Real Estate, Transportation,

Telecommunications, Utilities, Automobiles, and Household & Personal Products. Banking, Finance, Insurance, Investment companies, and closed-end mutual funds are excluded because their regulatory frameworks, financial structures, and liquidity characteristics differ substantially from those of other listed companies. Only firms that remained continuously listed throughout 2021–2025 and had the required information available were included to ensure consistency and reliability of the data.

The study relies on secondary data collected primarily from the annual reports and financial statements of the selected companies for the period 2021–2025. Information relating to corporate governance mechanisms is obtained from the corporate governance sections of annual reports, while financial information required to measure corporate cash holdings and other study variables is extracted from the companies reported financial statements. Additional information is obtained from publicly available CSE disclosures where necessary. The collected data are systematically organized into a panel dataset to ensure consistent measurement of the variables across firms and years and to facilitate the empirical analysis.

The relationship is tested using regression model illustrated in equation 1. In the equation, MO is managerial ownership, IO is institutional ownership, BI is board of independence, BM is board meeting, BS is board size, FS is firm size, LEV is leverage, G is growth and $\varepsilon_{it}$ is the error term for firm i in year t.

$$CH_{it} = \beta_0 + \beta_1 MO_{it} + \beta_2 IO_{it} + \beta_3 BI_{it} + \beta_4 BM_{it} + \beta_5 BS_{it} + \beta_6 FS_{it} + \beta_7 LEV_{it} + \beta_8 G_{it} + \varepsilon_{it} \text{ ---(1)}$$

## 4. Results and findings

Descriptive statistics are provided in Table 2, Institutional ownership averages 76.96% highlighting active institutional involvement, which supports long-term value creation. Independent directors account for 43.9% of board members on average aligning with Sri Lanka's Code of Best Practices on Corporate Governance (2017). However, this proportion is lower than in developed markets such as the U.S. (54%) and Malaysia (50%). Board size averages eight directors, meeting the optimal range of eight to nine directors suggested by Lipton and Lorsch (1992). This trend is consistent with emerging markets like Malaysia but smaller than the U.S. average of 12.25 directors (Yermack, 1996). The average number of board meetings is 5.142. Debt-to-equity ratios average 0.509 reflecting diverse financial structures.

As presented in Table 3, managerial ownership demonstrates a weak negative correlation with cash holdings ($r$ = -0.10418, $p$ = 0.001). These results of this study are in line with research conducted by Ahmed et al. (2018), Mawardi and Nurhalis (2018), Talbi and Menchaoui (2023). Institutional ownership, on the other hand, exhibits a weak but significant positive association with cash holdings ($r$ = .048, $p$ = .028), suggesting that higher institutional shareholdings are associated with increased cash reserves. Prior studies (e.g., Huang & Zhu, 2015; Aggarwal et al., 2011) support this finding, emphasising the role of institutional investors in enhancing governance, reducing equity costs, and driving innovation, thereby supporting long-term value creation. Board independence displays a

significant negative relationship with cash holdings ($r$ = -.011, $p$ = .035), reinforcing findings from earlier research (e.g., Boubaker et al., 2015; Hassanein & Kokel, 2019). Independent directors are more likely to mitigate agency risks by discouraging excessive cash reserves. Conversely, board meetings and board size show insignificant relationships with cash holdings ($r$ = -.014, $p$ = .665; $r$ = .043, $p$ = .175, respectively), indicating limited associations. Nonetheless, prior literature highlights the strategic and oversight roles of these governance attributes (e.g., Dalton et al., 1999; Lipton & Lorsch, 1992). Similarly, Abuhijleh and Zaid (2023), Ajanthan and Kumara (2017), and Hassanein and Kokel (2019) found that the frequency of board meetings and board size do not significantly influence cash holdings. Among the control variables, leverage exhibits a positive correlation with cash holdings ($r$ = .243, $p$ < .001), while firm size shows a significant negative association (r = -.046, $p$ =.048), and growth rate reflects an insignificant negative link ($r$ = -.021, $p$ = .508).

**Table 2: Descriptive statistics**

| Variables | Obs | Mean | Std. Dev. | Median | Max. | Min. |
|---|---|---|---|---|---|---|
| Cash Ratio (CR) | 1000 | .089 | .121 | .043 | 1.000 | .000 |
| Managerial ownership (MO) | 1000 | .066 | .158 | .001 | .850 | .000 |
| Institutional ownership (IO) | 1000 | .770 | .434 | .860 | .9777 | .000 |
| Board of independence (BI) | 1000 | .439 | 1.573 | .375 | .5000 | .167 |
| Board Size (BS) | 1000 | 8.686 | 2.347 | 8.000 | 19.000 | 4.000 |
| Board meeting BM | 1000 | 5.142 | 2.157 | 4.000 | 17.000 | .050 |
| Leverage (LEV) | 1000 | .509 | .806 | .480 | 24.794 | .013 |
| Firm size (FS) | 1000 | 23.428 | 1.410 | 23.363 | 27.336 | 19.136 |
| Growth (GR) | 1000 | .256 | 1.948 | .082 | 57.070 | -.908 |

**Table 3: Correlation Matrix**

| | CR | MO | IO | BI | BM | BS | DE | FS | GR |
|---|---|---|---|---|---|---|---|---|---|
| CR | 1.0000 | | | | | | | | |
| MO | -.1042 | 1.0000 | | | | | | | |
| | *(.0010)* | | | | | | | | |
| IO | .0481 | -.3705 | 1.0000 | | | | | | |
| | *(.0284)* | *(.0000)* | | | | | | | |
| BI | -.0107 | -.0195 | .0081 | 1.0000 | | | | | |
| | *(.0345)* | *(.5382)* | *(.7973)* | | | | | | |
| BM | -.0137 | .0413 | -.1237 | -.0055 | 1.0000 | | | | |
| | *(.6651)* | *(.1917)* | *(.0001)* | *(.8634)* | | | | | |
| BS | .0430 | .1488 | -.0122 | -.0144 | .2713 | 1.0000 | | | |
| | *(.1748)* | *(.0000)* | *(.7010)* | *(.6495)* | *(.0000)* | | | | |
| DE | .2432 | .0128 | .0060 | -.0100 | -.0175 | .0329 | 1.0000 | | |
| | *(.0000)* | *(.6866)* | *(.8492)* | *(.7524)* | *(.5805)* | *(.2985)* | | | |
| FS | -.0458 | .1430 | -.1072 | -.0304 | .1470 | .1205 | .0509 | 1.0000 | |
| | *(.0480)* | *(.0000)* | *(.0007)* | *(.3373)* | *(.0000)* | *(.0001)* | *(.1075)* | | |
| GR | -.0209 | -.0156 | .0006 | -.0040 | -.0427 | -.0340 | -.0197 | .0600 | 1.0000 |
| | *(.5083)* | *(.6234)* | *.(9846)* | *(.9002)* | *(.1772)* | *(.2828)* | *(.5347)* | *(.0580)* | |

*Note: p-values are in italics inside parentheses*

Variance Inflation Factor (VIF) values range from 1.345 for Board Independence to 4.250 for Managerial Ownership. All centered VIF values are below the commonly accepted threshold of 5, indicating that there is no serious multicollinearity among the explanatory variables. Although Managerial Ownership records the highest VIF (4.250), it remains within the acceptable range. The relatively high uncentered VIF values for some variables do not indicate problematic multicollinearity, as the centered VIF is the appropriate measure for assessing relationships among the explanatory variables. Therefore, the results confirm that the governance variables and control variables can be included in the regression model without substantial multicollinearity concerns.

**Table 4: Multicollinearity test**

| Variable | Coefficient variance | Uncentered VIF | Centered VIF |
|---|---|---|---|
| Constant | .65841 | 6543.98740 | NA |
| Managerial Ownership | .05442 | 7.06515 | 4.250156 |
| Institutional Ownership | .06532 | 51.2949 | 3.578101 |
| Board Independence | .06582 | 18.8590 | 1.345105 |
| Board Meetings | .04785 | 15.2743 | 2.253610 |
| Board Size. | .00028 | 6.25631 | 1.468744 |
| Leverage | 1.01459 | 3549.08 | 3.178798 |
| Growth | .58942 | 4522.24 | 2.403459 |

Table 5 outlines the findings of three regression models, namely the random effects, fixed effects, and ordinary least squares (OLS) models employed to evaluate the impact of various determinants on cash holdings. The independent variables include ownership structure, represented by institutional ownership and managerial ownership, as well as board structure, measured through proxies such as board size, the composition of independent directors, and the frequency of board meetings. Additionally, the analysis incorporates control variables, including firm size, leverage, and growth, to provide a comprehensive understanding of the factors associated with cash holdings. Based on the Hausman test, the fixed-effects model was deemed the most suitable ($x^2$=5.2079, $p < .050$). The model's *R*-squared value reveals that 70.94% of the variance in cash holdings (CH) is explained by the independent variables, while the adjusted *R*-squared of 67.45% indicates that the model retains substantial explanatory power after accounting for the number of predictors. The model is statistically significant, as evidenced by the *F*-statistic of 20.3513 ($p < .001$). The Durbin-Watson statistic of 1.107082 suggests the possibility of positive autocorrelation in the residuals.

Notably, managerial ownership (MO) indicates a statistically significant negative association with CH ($\beta = -.042$, $p = .049$). This means that a one-unit increase in MO is associated with a .0418-unit reduction in CH, holding other variables constant. These results align with prior studies (Morck et al., 1988; McConnell & Servaes, 1990; Ozkan & Ozkan, 2004), which theorise a non-linear relationship between managerial ownership and cash holdings. At lower levels of managerial ownership, the alignment effect prevails, reducing cash holdings as managers' interests align with those of shareholders. Conversely, at higher levels, the entrenchment effect may occur, leading to higher cash reserves as managers prioritize personal interests. In the Sri Lankan context, where firms typically have low managerial ownership due to the dominance of institutional and public ownership, the

alignment effect is more evident. This is consistent with findings from Ahmed et al. (2018), Mawardi and Nurhalis (2018), and Talbi and Menchaoui (2023), which confirm a significant negative correlation between managerial ownership and cash holdings. Thus, as managerial ownership increases, agency costs are reduced, and cash holdings decline, supporting the acceptance of hypothesis $H_1$.

**Table 5: Regression results**

| Variable | OLS | Random Effects | Fixed Effects |
|---|---|---|---|
| MO | -.0803 | -.0669 | -.0418 |
| | (.0019) | (.0464) | (.0488) |
| IO | .0037 | .0014 | .0019 |
| | (.0375) | (.0322) | (.0077) |
| BI | -.0007 | -.0006 | -.0006 |
| | (.0469) | (.0098) | (.0418) |
| BM | -.0001 | .0000 | -.0005 |
| | (.9698) | (.9835) | (.8131) |
| BS | .0220 | .0031 | .0049 |
| | (.1876) | (.1447) | (.0536) |
| DE | .0365 | .0376 | .0379 |
| | (.0000) | (.0000) | (.0000) |
| FS | -.0048 | -.0071 | -.0095 |
| | (.0074) | (.0879) | (.0587) |
| GR | .0014 | .0000 | .0003 |
| | (.4591) | (.0048) | (.0521) |
| R-squared | .0755 | .1439 | .7094 |
| Adjusted R-squared | .0680 | .1370 | .6745 |
| F-statistic | 10.1162 | 20.8205 | 20.3513 |
| | (.0000) | (.0000) | (.0000) |
| Durbin-Watson stat. | .3540 | .9995 | 1.1071 |
| Chi square ( Hausman Test) | | | 5.2079 |
| | | | (.0351) |

*Note: p-values indicate within parentheses.*

The coefficient of institutional ownership (IO) is ($\beta$ = .0019, $p$ = .008), indicating a positive and significant association with cash holdings (CH). Prior research supports this finding; Zhang and Kyaw (2017) and Masry (2016) highlighted a positive relationship between institutional ownership and firm performance, demonstrating how institutional oversight mitigates agency conflicts and enhances corporate governance. Similar studies (Hesti Anita, 2019; Mawardi & Nurhalis, 2018; Masood & Shah, 2014; Al Najjar & Clark, 2017) emphasise that institutional ownership improves cash management, preventing excessive reserves while maintaining optimal liquidity. Thus, hypothesis $H_2$ is accepted.

Board independence (BI) indicates a significant negative association with cash holdings (CH) ($\beta$ = −.0006, $p$ = .042). Consistent with this finding, Belghitar and Khan (2013) observed a similar negative relationship between board independence and cash holdings among UK SMEs. Independent directors play a vital role in challenging management and influencing strategic decisions, as argued by Dowell et al. (2011). When management's discretionary control over cash is restricted, firms tend to maintain lower cash reserves. Agency theory suggests that large cash holdings can encourage opportunistic behaviour from management (Hassanein & Kokel, 2019), but an effective and independent board can mitigate

this risk by limiting excess cash reserves (Abuhijleh & Zaid, 2023). This study's findings align with previous research (Boubaker et al., 2015; Kusnadi, 2011; Cambres et al., 2022; Pranadita & Harymawan, 2020; Talbi & Menchaoui, 2023), which underscores the role of independent boards in managing corporate cash holdings effectively. As the proportion of independent directors increases, managerial discretion over cash holdings is curtailed, leading to more optimal cash management. These results support hypothesis $H_3$.

The study finds a negative but statistically insignificant relationship between the frequency of board meetings (BM) and cash holdings (CH), as evidenced by a coefficient value of ($\beta = -.001$, $p = .813$). Board meetings, which are formal gatherings of directors to deliberate on critical strategic matters, are generally expected to enhance oversight and reduce cash reserves (Hassanein & Kokel, 2019). These findings align with prior research by Ajanthan & Kumara (2017) and Hassanein & Kokel (2019), which similarly concluded that board meeting frequency has no significant effect on cash holding decisions. However, the results diverge from studies by Abuhijleh & Zaid (2022), which observed a significant reduction in cash reserves with more frequent board meetings, and from research by Abuhijleh & Zaid (2023) and Ezeani et al. (2023), which suggested that increased meetings lead to higher cash holdings. Therefore, hypothesis $H_4$ is rejected.

The study reveals a positive but statistically insignificant relationship between board size (BS) and cash holdings (CH), as indicated by the coefficient value of ($\beta = .005$, $p = .054$). While prior research has highlighted the advantages of a larger board, such as increased opportunities to engage with external stakeholders who control critical resources (Abeysekera, 2010; Musteen et al., 2010) and enhanced diversity in financial expertise, which strengthens the firm's image and stakeholder relationships (Chouaibi et al., 2021), these benefits did not yield significant results in this study. The findings suggest that while a larger board can contribute to cautious management oversight and higher cash reserves, potentially safeguarding shareholder interests it may also reflect weak governance due to inefficient decision-making processes. This aligns with prior studies (Azis et al., 2021; Cambrea et al., 2022; Gul et al., 2020; Hassanein & Kokel, 2019; Ferreira & Vicente, 2020), which similarly observed higher cash holdings associated with larger boards. However, consistent with research by Darma et al. (2021), Kengatharan (2017), Pranadita and Harymawan (2020), and Rafinda et al. (2018), this study concludes that board size has no significant impact on cash holdings. Thus, hypothesis $H_5$ is rejected.

The analysis of control variables reveals significant relationships with cash holdings (CH). Leverage shows a positive and significant association with CH, with a coefficient of ($\beta = .0379$, $p < .001$), indicating that firms with higher debt levels tend to maintain larger cash reserves as a precaution against financial uncertainties. This reflects the precautionary motive, as leveraged firms retain cash to ensure stability and meet debt obligations during adverse conditions. Conversely, firm size has a negative but statistically insignificant association with CH, with a coefficient of ($\beta = -.0095$, $p = .059$). Larger firms typically hold less cash due to their enhanced access to external financing, stable and diversified cash flows, economies of scale in cash management, and market power to negotiate favourable payment terms.

In addition to that, pressure from investors to avoid inefficient cash hoarding encourages larger firms to operate with lower cash reserves, aligning with the trade-off theory, where firms balance the flexibility of cash holdings against their opportunity costs. These findings are consistent with studies by Abuhijleh and Zaid (2023), Ajanthan and Kumara (2017), Darma et al. (2021), Ezeani et al. (2023), and Kengatharan (2017). Meanwhile, growth rate has a positive but statistically insignificant association with CH, as shown by ($\beta = .0003$, $p = .052$). While growth can drive a need for liquidity, growing firms often prioritize reinvestment into expansion opportunities or rely on external financing, resulting in minimal or insignificant changes to cash reserves. This behavior reflects their focus on balancing immediate growth demands with available cash, rather than holding excess liquidity. Overall, the findings highlight that leverage significantly boosts cash holdings, firm size significantly reduces them, and growth rate exerts an insignificant positive effect, offering insights into the dynamics of cash management within firms.

## 5. Conclusion and Implications

The findings demonstrate that corporate cash holdings are determined not only by firms' financial characteristics but also by the governance and ownership environment through which financial resources are controlled. In particular, the significant effects of managerial ownership and institutional ownership indicate that who exercises ownership and monitors rights matters for corporate liquidity decisions. These findings are especially relevant within the Sri Lankan corporate setting, where ownership structures and the concentration of influence among major shareholders can shape managerial incentives and the monitoring of corporate resources. The results therefore suggest that ownership-based governance mechanisms may have a more observable association with cash-holding behaviour than certain board-level structural characteristics.

The insignificant relationships identified for board size and board meetings provide an important additional insight. Although the Sri Lankan corporate governance framework places considerable emphasis on effective boards, regular board engagement, accountability and appropriate oversight, the empirical evidence indicates that the numerical size of the board and the frequency of meetings alone may not be sufficient to explain variations in corporate cash holdings. The finding is consistent with the broader distinction between the formal presence of governance mechanisms and the effectiveness with which those mechanisms are implemented. The 2023 Corporate Governance Code emphasises that boards should provide effective direction, control and leadership, while also exercising independent judgement and ensuring appropriate systems of internal control and risk management. Similarly, the revised CSE Corporate Governance Listing Rules introduced enhanced requirements concerning board responsibilities, committees, risk management, internal controls, disclosures and related-party oversight. Therefore, the insignificant coefficients for board size and board meetings should not be interpreted as evidence that boards are unimportant; rather, they indicate that structural board characteristics by themselves may not adequately capture the quality and effectiveness of governance in controlling corporate liquidity.

From a theoretical perspective, the study contributes to the understanding of corporate cash-holding behaviour by integrating governance considerations with the financial motives underlying cash retention. Agency theory provides a particularly relevant explanation because cash represents a relatively flexible corporate resource that may create opportunities for managerial discretion when monitoring and incentive alignment are inadequate. The significant influence of managerial and institutional ownership provides empirical support for the argument that ownership arrangements can alter the incentives and monitoring processes surrounding the accumulation and use of cash. At the same time, the Keynesian, financing hierarchy, and trade-off perspectives provide complementary explanations for cash retention arising from transaction requirements, precautionary motives, financing flexibility, investment opportunities and the costs associated with external financing. Taken together, these perspectives indicate that cash holdings are not simply a liquidity outcome, but a multidimensional financial decision shaped by the interaction between governance, financing conditions, investment requirements and precautionary considerations. The study consequently extends the governance–cash-holding literature by providing evidence from the Sri Lankan listed-company environment, where institutional and ownership characteristics operate within a distinctive regulatory and corporate governance framework.

The findings also have important implications for Sri Lankan corporate governance practice. The CSE and SEC governance framework places increasing emphasis on accountability, transparency, board responsibilities, internal controls, risk management, shareholder relations and related-party transaction oversight. The SEC states that the revised governance requirements introduced in 2023 were intended to strengthen board and management practices and enhance investor and stakeholder confidence in the Sri Lankan capital market. In this context, the present findings suggest that compliance with governance requirements should be accompanied by substantive monitoring of financial resources. In particular, companies should ensure that cash-retention policies are clearly connected to operating requirements, planned investment, debt servicing, risk management and other identifiable financial objectives. Boards should therefore consider not only the level of cash maintained but also the rationale, expected use and opportunity cost of accumulated cash.

For managers, the findings imply that cash policies should be developed within a clearly defined financial framework rather than through discretionary accumulation. Management should periodically assess whether existing cash balances are justified by operating needs, investment opportunities and financing requirements, while excess liquidity should be evaluated in relation to shareholder value and alternative uses of funds. Institutional investors can also contribute to stronger governance by scrutinising management explanations for unusually high or persistent cash balances and by engaging with companies regarding the allocation and deployment of excess liquidity. Such monitoring is particularly relevant where institutional shareholders possess sufficient influence to question managerial decisions and encourage greater accountability.

The study also provides implications for regulators and market institutions. For the SEC, the findings highlight the importance of continuing to emphasise the effectiveness of governance practices, rather than relying solely on formal compliance with governance

structures. The SEC may further encourage disclosures that enable investors to understand significant cash accumulation, the intended use of excess liquidity, and the governance processes through which major liquidity decisions are monitored. This would complement the existing emphasis on transparency, accountability, internal controls and risk management within the regulatory framework. For the CSE, the findings support continued attention to the quality and clarity of corporate governance disclosures under the Listing Rules, particularly where ownership arrangements, board oversight, related-party considerations and financial-resource management may affect shareholder interests. The objective should not be to prescribe a single optimal level of corporate cash, since appropriate liquidity differs across firms, but to promote sufficient transparency for investors to evaluate whether cash-retention decisions are economically justified and appropriately governed.

The significant relationships observed for firm size, leverage and growth further demonstrate that governance mechanisms do not operate independently of firms' financial circumstances. Larger firms may possess greater operational and financial complexity, highly leveraged firms face different liquidity and financing pressures, and growing firms may retain cash to support expansion and investment opportunities. Accordingly, corporate cash policies should be interpreted within the broader financial context of each firm rather than assessed solely through governance characteristics. This reinforces the value of combining governance-based explanations with established financial theories when examining corporate liquidity decisions.

Despite these contributions, the study has several limitations. The analysis is restricted to selected companies listed on the CSE and covers the period 2021–2025; therefore, the findings may not necessarily extend to unlisted firms, smaller firms, or companies operating under different institutional environments. In addition, the study focuses on selected governance mechanisms and does not encompass all dimensions of corporate governance that may influence cash policies. Future research could therefore incorporate variables such as board independence, board diversity, director expertise, CEO characteristics, ownership concentration, CEO duality, audit committee effectiveness and the quality of board oversight. Further studies could also examine whether economic uncertainty, financing constraints, financial crises, technological transformation and changes in regulatory requirements modify the relationship between governance and corporate cash holdings. Comparative studies involving other emerging markets would additionally help determine whether the observed relationships are specific to Sri Lanka or reflect broader patterns in emerging capital markets. Employing dynamic panel techniques, instrumental-variable approaches or other methods capable of addressing potential endogeneity would also provide stronger evidence regarding the direction and persistence of the relationships identified.

Overall, this study establishes that corporate cash holdings should be understood not simply in terms of how much liquidity a firm retains, but also in terms of who influences that decision, how the decision is monitored, and why the resources are retained. The evidence from Sri Lankan listed companies over 2021–2025 indicates that ownership-based mechanisms, particularly managerial and institutional ownership, are significantly associated with cash-holding decisions, whereas board size and board meeting frequency do not exhibit

significant relationships within the model. These findings contribute theoretically by connecting agency considerations with the Keynesian, financing hierarchy and trade-off explanations of cash retention; practically by highlighting the importance of disciplined cash policies and meaningful shareholder monitoring; and from a policy perspective by reinforcing the relevance of effective governance, transparency and accountability within the CSE and SEC regulatory environment. The central implication is therefore not that a particular governance structure guarantees an optimal cash balance, but that effective governance should ensure that corporate liquidity is accumulated for identifiable financial purposes, monitored appropriately and deployed in a manner consistent with long-term shareholder and corporate interests. In this respect, strengthening the substance of governance alongside formal compliance can contribute to more transparent, accountable and value-oriented cash-management practices within Sri Lanka's capital market.

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