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Rebalancing the Corporate Governance & Role of Indifference Theory: A Way of taking the Stress out with Substitute Mechanism

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Abstract
We provide the rational and theorem of rebalancing the corporate governance and taking the stress out with substitute mechanism explains whether the insider ownership and leverage can be considered as substitute mechanism to reduce the agency cost, which means we are indifferent either using financial leverage or insider ownership to control the agency cost. Assuming other things constant; such as magnitude of effect on agency cost & adding debt could create direct and indirect bankruptcy risk. We utilize a sample of 41 firms from the SBP/SDWD database and find an influential rebalancing agency approach under the shadow of indifference theory. Hence, this study answers the question that insider ownership and leverage can be considered as substitute appliance or mechanism geared at reducing the effect of agency cost.
Keywords: Indifference theory; Governance liberalization; Insider ownership; Substitution mechanic; Leverage; Asymmetric information

1. Introduction

The assessment of corporate governance system of a company along with interest's conflicts and operations' transparency has progressively turn into essential factor in the process of investments' decisions. Many company's failures common thread is weak corporate governance (Barle & Means, 1932). Board of directors' inadequate oversight, managers' diverse ambitions, destruction of minority shareholders, and improper rights protections of creditors can unsettle any leading company. In the 1990, burst of bubble edged to severe interest's conflicts by analysts and brokers. Practices of poor corporate governance steam the accounting scandals and high profile corporate bankruptcies by past several decades and significantly unrecompensed to the financial crises 2008.

Shareholders' objective is their investment returns, managers likely to have diverse ambitions, like esteem and prestige to run powerful and large organization, perquisites and diversion of their position. Control & separation of ownership in a large firm provides the floor for managers to create agency conflicts and to strive their own interest rather than shareholders' value maximization. Barle & Means (1932) traced the prospects of owners and managers interests' conflicts outlined by their classical theory of "ownership's separation from control." Instead of firm's value maximization managers have motive for their own utility maximization or also used the resources of firms for their own particular benefits, that's why agency cost increases because of separation of control and ownership (Jensen & Meckling, 1976). It may be possible that the managers may invest over and above the level which is set as an optimal level and for the purpose of expansion. The result of overinvesting in business is that manager raises resources which are under their control for self-aggrandizement. At the time when firm expands in size, managers' gain more power, consequently greater opportunities to enjoy excessive perks and perquisites (Jenson, 1986).

Capacity of debt allow the investor to regulate managers and also allow investor that they can collect the information which is useful for oversee management (Raviv and Haris, 1990). Debt holder gives stress to managers so they provide detailed information because they have this legal right. The investor can also use this information to control the manager's activities. Adding debt will lead into bankruptcy risk, bankruptcy risk may provide motivation for the improvement of management. Manager enjoy the bankruptcy threat which will bring more stress on managers (Grossman & Hart, 1982). Because of tough disclosure points and offer more rights to creditor's international debt contracts had strong effect of monitoring. Additionally, managers and directors' ownership results in reduction of unwanted perks and perquisites (Havery. Et al, 2004).

Larger chunk of shares held by managers as they identified common interest with owners. Since, conflicts' nature between owners and managers and its economic consequences exhibited in the classical theory using the corporate governance structure of Anglo Saxon (Barle & Means, 1932). A firm's owners and its management and ownership widely diluted among shareholders, so that monitoring management carefully do not have a strong incentive, company's shares do not held by the managers in larger fractions resulting in mismatching financial interests.

Jensen and Mecklig (1976) proposes higher insider ownership and financial leverage mitigates agency costs. Consequently, insider equity ownership and leverage can be considered as substitute appliance or

mechanism geared at reducing the effect of agency cost. Excessive debt uses results in bankruptcy risks increases, henceforward, greater the increased bankruptcy risk, lower the willingness of top managers to admit increased financial risks (Steiner & Chen, 1999). Managers of firms carrying the higher insider ownership struggle to bypass diluting their power and control by adding debt (Sorensen and Kim, 1986). Jensen and Meckling (1976) drawn attention that financial leverage and insider ownership are simultaneously determined in order to minimize total agency cost which is incurred in investment decisions and external financing.

If both serves as substitute tools geared at reducing agency costs, higher the level of insider ownership should lead to lower the levels of financial leverage, and vice versa, and higher the level of insider ownership or leverage expected results the lower the agency cost and vice versa.

1.1 Theoretical Base

Practices of corporate governance differ among the jurisdictions and countries and even within country different systems of corporate governance may exist. In most of the world, systems adopted of corporate governance typically reflect the impact of stakeholder or shareholder theory, as well as cultural, political, historical, legal and other impacts which is specific to a region. In response to accounting scandal early in 2000, regulations similar to US, like Sarbanes Oxley Act 2002 implemented by number of countries for investors' confidence restoring and improving internal controls in financial disclosure. In 1990, two reports were published, Principles of Corporate Governance and the Cadbury Report in distinctly influential in streamlining the landscape of corporate governance with the central theme of shareholder theory and agency conflicts.

Likewise, OECD (Economic Cooperation and Development) in 1999 generate the Corporate Governance Principles which expand the context of corporate governance by considering the other stakeholders' interests, importantly creditors, employees and suppliers. Corporate Governance Principles were revised and updated in 2004 and once more in 2015 by examining the potential positive reactions including economic stability and financial market growth and designed the guidelines and standards to improve and evaluate framework of corporate governance throughout the world.

1.1.2 Corporate Governance and Shareholders' Theory

Shareholder theory proceeds the picture that company's manager most important and prime responsibility is to maximize the returns and value of shareholders as well as prime objective of this study. The relationship of principal and agent involves trust, obligations and loyalty. As discussed the traditional shareholder's theory earlier, act in the shareholders' best interest is the prime duty of managers by equity value maximization. Relationship of principal-agent often involve into conflicts, managers may pursue to maximize their perquisites, power and remuneration. Interests' of Manager and shareholder can also digress on the subject of risk tolerance. Shareholders may have comparatively high risk tolerance due to diversified investment portfolio. However, directors and managers in their corporate decision making are more risk averse so their employment status could be better protected by them. Corresponding behavior may diverge from the value creation objective of the firm. Additionally, managers to information about the business about the firms operations have greater access than the shareholders which is access to information is unequal, such as "Information Asymmetry", makes it painless for managers to make the decisions that are against the shareholders' interest and diminish the shareholders' ability to execute control.

Likewise, another interest's divergent might arise between directors and shareholders when insiders influence the board. Consequently, board's ability may hindered to properly perform its control and monitoring. Finally, if certain influential shareholders are favored over minority shareholders resulting in conflicts among two groups. Managers favor to increase the firm's size even it harms the shareholders' interests, as considerably managers prestige and remuneration are positively connected to firm size which direct to interests confliction between shareholder, who are associated towards their shares' value maximization, and managers, who clinch to value expansion (Murphy, 1985). Worst case scenario under surplus fund, managers tend to undertake the insecure project which would be refused by the capital market.

However, to limit the conflicts between shareholders and managers several mechanisms served under the agency theory framework of corporate governance for the both groups to align the interest. Certain controls and powers are granted to shareholders by the traditional corporate governance mechanism and corporate law. The participation in general meetings by the shareholders, the most effective tool, to execute their voting rights on major cooperate transactions, board elections and matters to force the management to match their interests with shareholders. Board performance is monitor by the shareholders through the participation in general meetings and exercise of voting power. The board principally obliged to shareholders and liable for firm's proper governance, on this note, board is the bridge between managers and shareholders to align and protect the shareholders' interests. The board also administer the functions of film's control, audit, and risk management to ensure the compliance with the applicable regulations, laws and proper governance system adoption. Limiting the freedom of actions of managers has a decisive aspect to play in diminishing the equity agency cost and free cash flow reduction is recommended as a solution (Jenson, 1986). According to this theory, shares repurchases,

dividend payout and extra debt handle to reduce the excessive cash flows under managers' control and unprofitable oriented expansions reduction.

Furthermore, remuneration plans of executive have attain the sound concerns in the investment world, aiming the shareholders and managers interests alignment is the preliminarily goal, so, incentive plans typically stock options and profit sharing on performance. It must also consider shareholders dilution theory takes place with the new stock issuance if the sufficient control associated with the new issuance. Besides the traditional corporate governance mechanism to limit the conflicts between shareholders and manager, bankruptcy provide incentive for the improvement of management which is also central theme of our study. Bankruptcy threat will bring more stress on managers to reduce the over-investment dilemma. Debt reduce the agency cost through systematical decisions making and management monitoring involvement.

2. Literature Review

(Ang.et.al, 2000) defined the impact of structure of ownership on agency cost by the usage of data and insider equity ownership of small businesses. They investigated that by alignment of managers and shareholders interest and with outside monitoring by banks agency cost decreases. This fixates stress on managers to provide the real report of business to the investors of such financial institutions and to run the business profitability. This control and monitoring also reduces the agency cost of owner and manager. With the usage of small businesses the results investigated that when there is increase in non-managers owners the agency cost increases. When an outside manager manages the firm the agency cost becomes high and with the share of manager in ownership it becomes negatively related

A large quantity of other researchers had considered the impact of other factors which could lessen agency cost. Jensen and meckling in 1976 defined that large shareholders had extra influence and are more provoked and also investigated they can lessen the agency cost by bringing into line the interest of shareholders and managers. Likewise, the results of (Shleifer & Vishny, 1986) shows that large shareholders had inducement to control and regulate the managers and be able to alleviate the problem of agency. Though, the study of (Nekhili, et al 2009) investigated that the concentration of ownership increased the agency cost of cash flow by the usage of sample data of small businesses.

The study of Ang et al (2000) is extended by Singh and Davidson, to the large American corporations. Their results of the study showed that insider ownership reduces agency cost when they utilized assets utilization but the relationship is insignificant when discretionary expense ratio is used because they used the proxy of asset utilization and discretionary expense ratio for the measurement of agency cost (Singh and Davidson, 2003).

In a study of (Havery. Et al, 2004) by usage of data of 18 emerging markets explores the impact of leverage and directors' equity ownership on governance. The results demonstrated that because of tough disclosure points and offer more rights to creditor's international debt contracts had strong effect of monitoring. Additionally, managers and directors' ownership results in reduction of unwanted perks and perquisites. The firm that has some opportunities of growth and the problems of overinvestment, the debt and insider equity ownership is more beneficial dive in firm.

By replicating the study of (Ang. Et al 2000) the author uses the sample data of SME's of Australia. For agency cost they used the proxy of asset utilization ratio and operating expense ratio. In their study they test the relationship of debt (solely banks loans) to managerial equity ownership and on agency cost, the results demonstrated that there is no significant shock on discretionary operating expenses but asset utilization is improved by leverage. In addition to that, both debts and insider ownership work as mitigating agency cost (Fleming et al 2005).

By using the panel data (Kale et al 2007) find out the relationship among employee productivity and leverage in order to examining the regulation of debt. The results of study predicts that with leverage productivity is associated positively at the lower level of leverage but this relationship turn into negative when the leverage becomes adequately far above the high. According to study, higher level of debt financial distress cost turn into large which compel employees to search for any other job and as a result the strength of productivity of employees becomes low and this is the reason of above negative relation.

A study results shows that the agency cost aid negatively related to leverage and manager's ownership, by using multivariate and univariate method and investigate the effect of leverage and ownership of managers on agency cost by using a sample of 323 UK firms. Anyhow, the results of univariate analysis demonstrate positive but insignificant relationship among agency cost and leverage. As a final point, whether the impact of leverage on the cost of agency turns good when at different leveraged phases becomes larger leverage differences of the firms, no significant indication were found. (Zhang and Li, 2008).

Beside the agency theory framework through insider ownership and debt, Ross (1977) explored the asymmetric information among firm's shareholders, managers and banks which is focused by the signaling theory. They assumed that firm's insiders have better information of future projects, investment opportunities and cash flows than outsiders. Therefore, and change in dividend policy, equity structure, structure of managerial

ownership and debt structure considered firm's performance signal by outsiders. Hence, adding debt interpreted the better future growth and higher cash flows. Contradicting, equity edition represent the unfavorable circumstances (Ross, 1977).

The literature with reference to block-shareholders' role soundly propose that external block-holders have motive to influence and monitor management properly to hedge their significant investments (Lang & Friend, 1988). These block-holders have substantial desire to monitor management diligently to ensure and certify that management do not enlist in block-holders' detrimental wealth activities by cause of their massive economic stake in the firm. Theory of 'Active Monitoring Hypothesis' pose that managerial opportunism's scope reduced by external block-holders resulting in mitigating management and shareholders direct agency conflicts (Vishny & Shleifer, 1986).

(Pound, 1988) has challenged the Shleifer and Vishny's 'Active monitoring hypothesis' theory and introduce the 'Passive voters' hypotheses. He contends that external block-holders may be in the passive voters' tier who collude with managers and other corporate insiders against the dispersed shareholders' best interest. McConnell and Servaes studied on the late theory of Pound 'Passive voters hypotheses' and evident the consistent result with Pound theory.

(Singh & Shome, 1995) carried out the evidence which is consistent with 'Active Monitoring Hypothesis'. They conduct the event study methodology to examine the reaction of the market on large share parcels acquisitions' announcement. In their study, they reported the shares acquisition announcement by block-holders has positive impact on abnormal returns. Furthermore, he concluded agency cost reduction is positively associated with abnormal returns. In addition to that, (Bethel et al, 1998) concluded in their study that activist block-holders improves long term operating performance.

(Stuart Locke, 2005) conduct the study on managerial ownership relation with leverage using the unlisted firms' panel data of New Zealand covering the window 1998 to 2009. He applied the Granger causality tests which shows the significant bi-directional relationship between managerial ownership and financial leverage. Additionally their findings suggest U-shaped an inverse relationship of managerial ownership and leverage, which indicates the lower insider ownership increases misalignment and higher ownership increase the entrenchment effect. Furthermore, his study proof the negative relation with firm's total debt. Hence, for value maximization and to reduce agency conflicts managerial ownership is better for firms which apply lower debt policy.

(Merck et al, 1988) propose that agency conflicts arises due to two opposing forces that derive the response from the corporate managers. Managers naturally concentrate on to allocate the resources of the organization to increase their own power, wealth and perquisites. This force create the misalignment of interest with external shareholders. He examine the insider ownership as a second force to solve such agency conflicts. He evident that, as equity ownership of managers increases, misalignment of the interest also decreases with external shareholders. Merck also figured out that is impossible earlier to anticipate at any level of managerial ownership, which force likely to dominate. Hence, the relationship between ownership structure and corporate value is an empirical issue.

(J. McConnell & Servaes, 1990) investigate the relation between structure of equity ownership and Tobin's Q. They formed the sample of 1,173 companies for 1976 & in 1986 standing with 1,093 companies. Their findings represent significant curvilinear association between corporate insider ownership and Q. Tendency is up word of this curve slop until managers' ownership attain 45% to 50%, beyond this slopes trend to down word slightly. In addition, they found the positive relation between institutional investors (block-holders) and Q ratio. Consequently, their study is consistent with the hypothesis of equity ownership structure influence the firm's value.

(Chichti & Fatma, 2011) examined the impact of ownership structure and debt policy on agency problem which begin due to overinvestment problem using the simultaneous equation approach and designed three stage square model. They studied at Tunisian listed companies covering the sample 35 non- financial firms. Their results revealed significant negative association between free cash flows and financial leverage, which notify that by issuing debt overinvestment problem could be reduced.

(Ahmad & Mushtapha, 2011) investigate the debt financing effect on monitoring cost in firms listed in Malaysia. Their results conclude that monitoring cost decreases as increase in debt. It is because, monitoring through banks makes managers more careful and conservative. Additionally, external audit cost increases than the cost of internal audit as debt financing increases. They supported the result with the argument that lenders desire independence third to audit financial to make sure that insiders are following debt covenants.

(Larcker & Core, 2002) investigate the firm performance through the target ownership plan which is the minimum or specific junks of stocks that must to hold by insiders. Their results showed that managerial equity and performance of the stock at low level before the execution of target ownership plan. Although, their result reported an improvement on assets' excess return after two years following the plan of minimum ownership plan. Hence, principle agent conflicts could be resolved through the specific level ownership plan.

Resembling further, Singh & Shome is further extended by Timothy J. Brailsford. They put forward a further link between block-holders ownership effect on capital structure. They used the agency framework in their study which explain that equity ownership distribution among external block-holders and corporate managers has significance influence on leverage. Various aspects of such relationship have been explored by testing four hypothesis in their study. Their study support the positive relation between block-holders ownership and leverage. Furthermore, they evident a curvilinear relationship between insider ownership and leverage. Their results are also parallel with Singh & Shome (Timothy J. Brailsford, 2000).

This study extends the literature by proposing a further link of substitution mechanism between insider ownership and leverage by considering that third party (Leverage or Debt holders) can reduce equity agency costs via management monitoring participation and providing more systematical decisions making. Furthermore, this study investigates the effect of change in leverage & insider equity ownership on agency cost mitigation.

3. Research Modeling

3.1 Data Sources and Sample Size

To execute econometric projection or estimation, data acquired from SBP/SDWD database covering the period of 2010 to 2014. Thus, the study constitute on secondary data. The reason of financial firms' exclusion i.e. Insurance, Banking, Modarabas & Leasing etc. from sample is that, this sector is highly regulated and are many restrictions and unique characteristics on its capital structure. Additionally, analysis of 41 non-financial companies clinching the five year financial data which led to 205 observations.

3.2 Model

Testing the hypothesis of panel data estimation approach takes account of hetroskedasticity (individuality) and endogeniety in the data. For the panel data estimation; (PRM) Panel Regression Model, (REM) Random Effect Model and (FEM) Fixed Effect Model are three key accessions.

The problem with Panel Regression Model is that it does not distinguish between the various companies that we have. In other words, e.g. by combining 41 companies by pooling, we deny the heterogegeneity or individuality that may exist among 41 companies.

Thus, The approach we taken up "Fixed Effect or Random Effect Analysis of Regression" to test effect of change in leverage & insider equity ownership on agency cost and indifference theory that mitigate the agency cost. We applied "Hausman Test" to check which model (Random Effect or Fixed Effect) is suitable to accept. This test report the null hypothesis "Coefficients are not different systematically or Random effect Model is appropriate". By applying the test, this hypothesis does not hold. Thus, we choose Fixed Effect Model.

Through FEM model we abled to dismiss omitted or missing variable bias, endogeniety and hetroskedasticity, hence confess for controlling across the sampled firms unobserved heterogeneity. The Fixed Effect Model allows to clinch the heterogeneity or individuality among all the companies by allowing to have its own intercept value. The case with Random Effect Model accounts a common mean value for the intercept for all the companies and it fluctuate from firm to firm that we have in our sample.

Table 1: Hsusman Test

	Chi^2-Stat	**Chi^2. d.f.**	**Prob.**
Model 1	10.48**	4	0.0331
Model 2	16.89*	4	0.002

**. Significant at the 5% level. *. Significant at the 1% level.

The systematical structural forms of equations to be estimated in the study follows.

$$AGNCit = \beta 0 + \beta 1INSIit + \beta 2LEVJit + \beta 3RMSit + \beta 4INSTOit + \delta i + eit \quad (1)$$

$$LEVJit = \beta 0 + \beta 1INSIit + \beta 2ROAit + \beta 3DDNDit + \beta 4INVit + \delta i + eit \quad (2)$$

AGNCit = the dependent variable of the model 1, for firm i at t period.
LEVJit = the dependent variable of the model 2, for firm i at t period.
δi = the firm-specific fixed effect

3.3 Definitions and Measurement of Variables

Thus, many other aspects which could affect the agency cost model and financial leverage model. Therefore, we have included the two control variable in our study in the agency cost model which is block holders' ownership and directors' remuneration structure. Additionally we considered three control variable determinants based on leverage model for the model sustainability that is investment, profitability and dividends.

LEVJ (Financial leverage): Leverage (Explanatory Variable: 1st model and Dependent Variable: 2nd model) grabbed by figuring out the debt ratio, which is "total liabilities" divided by "total assets".

INSI (Insider ownership): Insiders are firm's directors, managers, officers, relatives, association who have right to appoint the director with specific fraction of ownership to participate in the firm's management. Insider ownership (Explanatory or Independent Variable 1st & 2nd model) be dug through the ratio of "Shares

held by Insiders" to "total number shares issued", as a stand in or proxy for insider ownership.

AGNC (Agency cost): To dig agency costs (Dependent Variable in 1st model), we applied the alternative efficiency ratio mechanism could be enacted which periodically taken place in the accounting and financial economics, (James S 2000; Rabel A & Ang 2000; Cole, Wuh Lin, Davidson & Singh 2003).

Expense ratio: Operating expense / annuall sales

PRFT (Profit): High profitable firms incline to use of funds that are source of internally generated over externally generated like equity and debt, proposed by Majluf and Myers (1984) in "Pecking Order Theory". A presumption of this argument that amount of debt will be reduced by higher profitable firms, to finance its projects since internally generated funds are available.

Proxy of profitability cracked by ratio of "total profit" to "total assets" (ROA).

DDND (Dividend): Higher dividend catering firms which have bad or even sustainable record will demand and acquire additive funds form debt (Emmery & Finnerty, 1997). Supporting this argument, firms transmit a signal of rising the profitability by higher dividend (Miller & Rock, 1985). Moreover, to fund the artificial signal, extra leverage utilized in order to get optimal capital structure. Whereas, Agency conflicts could be reduce by making higher dividends payments (Rozeff, 1985), in addition to that, he finds the empirical negative relationship between leverage and dividend. Finally, by considering above empirical literature, we include dividend as control variable which will be expected to positively related to leverage.

INV (Investment): Leverage policy effected by firm's investing activities. Funds that are internally generated exhausted, firms to finance its projects and operations swings to external source of funds. Hence, an increment in financial activities will elevated firms to debt than equity as external financing source (Majluf & Myers, 1984) documented it in analysis of pecking order capital structure. Investment opportunity variable examined by the proxy of "capital expenditure" to "total assets", proposed by (Allie et al, 1993; Saputro, 2003; Sanz1, 2001; Chang, 2009).

Capital Expenditure = (fixed assets book value t - fixed assets book value t-1) / Total assets

RMS (Directors Remuneration structure): Prediction is made on prior literature investigation, lower the agency cost by increased directors' remuneration or incentives which pressure the managers to work and align their interest with stockholders of the firm. In contrast, (Darren Henry, 2006) documented the remuneration structure mechanism as negative influence on agency cost, which projecting agency cost does not mitigating by steeper remuneration structure. Monitoring through an engaged and freewheeling boards of directors notify that managers enact in the shareholders best interest (Fama and Jensen, 1983).

INSTO (Institutional Ownership or Block-Holder): 'Active Monitoring Hypothesis' pose that managerial opportunism's scope reduced by external block-holders resulting in mitigating management and shareholders direct agency conflicts (Vishny & Shleifer, 1986). Mitigating agency problem, decisive role played by institutional stockholders, who can influence decisions to be made by managers exposed by (Brickley, 1988; Lease & Smith, 2004; Henry, 1988). In divergence, institutional ownership do not geared to reduce agency cost (Doukas et al, 2000; Mcknight & Weir, 2008). Following Darren Henry (2006) Institutional ownership determined as slicing the total percentage stockholdings of all institutional stockholders.

Table 2: Summary of Variables, Definitions and Calculations

Variable	Measurement	Abbreviation
Leverage	Total Liabilities / Total Assets	LEVG
Insider Equity Ownership	Shares held by Insiders / Total equity issued: OR % given in Report	INSI
Profitability	Net Profit / Total Assets	ROA
Dividend	Dividends / Net Income	DDND
Investments	Fixed assets book value t - fixed assets book value t-1/ Total Assets	INV
Agency Cost	Operating Expense / Sales	AGNC
Directors Remuneration	(Natural Logarithm Sum of Director's Annual Benefits Paid)	RMS
Block-Holders	Number of Shares held by Block-Holders / Total Shares Outstanding	INSTO

4. Statistical Results and Analysis

4.1 Descriptive Statistics

Descriptive statistics on view in table 3 addressing the mean, maximum, minimum median values with standard deviation of eight variables for the period of 2010-2014. Sample of 41 firms have been taken listed in SBP/SDWD database. Notably, managers of sampled firms of PSE market on average own the .5959 (59.59%) which means this is quite higher than the U.S market's managerial ownership level reported in the study of Jsensen ei al (1992) and Dutta (1999).

Table 3: Summary of Descriptive Statistics

Variables	Mean	Median	Maximum	Minimum	Std.
AGNC	0.107512	0.080000	0.720000	0.000000	0.099154
INSI	0.595902	0.650000	0.950000	0.120000	0.186295
LEVJ	0.475707	0.470000	0.940000	0.010000	0.219125
DDND	0.145317	0.110000	2.250000	-2.870000	0.321158
INSTO	0.134683	0.100000	0.770000	0.000000	0.141811
RMS	17.20863	17.36000	21.13000	0.000000	2.032929
ROA	0.138098	0.110000	1.000000	-0.240000	0.200107
INV	0.032780	0.020000	0.270000	-0.120000	0.072196

4.2 Correlation Matrix

Table 4 presents the correlation matrix of all variables based on 41 firms' data for 2010-2014. In order to detect multicollinearity problem either exist or not among the regressors, the mechanism of Product-moment of Pearson correlation coefficient widely used (Kennedy, 1998). Multicollinearity exists when there is high correlation among the variables (Anderson et al, 2007; Saunders et al, 2003). Thus, through the use of correlation matrix technique, multicollinearity can be detected. Problem of multicollinearity will be existed among explanatory variables when a paramount correlation is composed among them. However, researches are diverged at specific benchmark correlation considered to be high. A correlation when exceed 0.80 will be consecrated high (Kennedy, 1998). Multicollinearity problem will exist when correlation among any two variables reached up to 0.80 (Cramer & Brayman, 2001). Whereas, Anderson proposed the 0.70 benchmark of high correlation (Anderson et al, 1999).

Whole sampled data being used to detect correlations between regressors using Pearson's r which is on view in table 4. Hence, it can be seen in the table that there is no severe correlation among any two of the explanatory variables, which marks multicollinearity in the study do not appear to pose a severe problem. Noteworthy, none of coefficients of correlation of all variables go beyond -0.46 or +0.32. Further analysis is drained to detect the type of association between variables.

Table 4: Correlation Matrix by Using Panel Data from 2010-14

	AGNC	INSI	LEVJ	DDND	INSTO	RMS	PRFT	INV
AGNC	1.0000							
INSI	-0.0529	1.0000						
LEVJ	-0.2523	-0.0648	1.0000					
DDND	-0.0330	0.1560	-0.2199	1.0000				
INSTO	-0.0551	-0.4655	-0.1384	0.0138	1.0000			
RMS	-0.1043	0.0577	-0.0526	0.1072	0.0810	1.0000		
ROA	-0.0152	0.1942	-0.2335	0.2849	-0/0584	0.3232	1.0000	
INV	-0.0707	0.0634	0.2703	0.0087	-0.0132	0.0845	-0.0086	1.00000

4.3 Regression Results

In order to investigate the corporate governance mechanisms to trim the agency cost and interrelationship of those mechanisms through panel data analysis. For the panel data estimation (REM) Random Effect Model and (FEM) Fixed Effect Model are key accessions. By means of this, the decision is planted to use fixed effect model on the basis of Hausman's Test and the results are obtained from the panel data by using FEM. However results are exhibited by table 5 and 6.

Table 5: Result with AGNC

	Specification	
	Fixed Effect Model	**Random Effect Model**
C	0.403332	0.314853
INSI	-0.18032**	-0.08070
LEVJ	-0.29398*	-0.21050*
RMS	-0.00072	-0.00204
INSTO	-0.26884*	-0.17731**
R2	0.649928	0.158059
Adj.R2	0.553659	0.141210
F-statistics	6.751124*	9.385868*

Table 6: Result with LEVJ

	Specification	
	Fixed Effect Model	**Random Effect Model**
C	0.866863	0.664112
INSI	-0.62073*	-0.29435*
ROA	-0.24167*	-0.22409*
DDND	-0.07838	-.0.09052
INV	0.717033*	0.948848*
R2	0.837618	0.309262
Adj.R2	0.792963	0.295447
F-statistics	18.75753*	22.38634**

***. Significant at the 10% level. **. Significant at the 5% level. *. Significant at the 1% level.

4.3.1 FE Regression Based on AGNC

Regression results are reported in table 5 by using the FEM, where AGNC is response variable. INSI displayed the negative relation with AGNC is significant at 5% which is consistent with the hypothesis of agency cost mitigation through insider equity ownership and proofing the theory of Jenson Meckling. Whereas, contradicting with the finds of Singh and Davidson (2003) who found the negative relation between managerial ownership and assets utilization ratio. Our study contradicting the entrenchment theory of Morck al (1988), Suk & Han (1998), Fama and Jensen (1983) and Demsetz (1983) which is managers perform well in moderate ownership but agency cost will be high in higher ownership tier. Thus, we also spotlight that at high level of insider ownership with a dominant stake in a firm where managers are less diversified and only incentive for the managers to increase shares holder wealth.

Furthermore, the regression outcomes reporting the highly significant negative relation between agency cost and leverage which is supported by numerous theories and consistent with the hypothesis. First, adding debt increased the monitoring of management, i.e. banks, and to put pressure to run firms profitable (And et Al, 2000). Second, debt crate the risk of bankruptcy risk and threaten the managers' job lost which considerably helps to align the managers and shareholders business interests (Williams, 1987; Gorossman & Hart, 1958). This outcome is also consistent with the study of Cui and Li (2003), Fleming et al (2010) and Hua et al (2010).

Since, many other aspects which could affect the agency cost. Therefore, we have included the two control variable in our study in the agency cost model. Hence, the results shows the fact that INSTO have negative relation with agency cost with the 1% level of significance. Similarly, Vishny & Shleifer (1986) investigate that shareholders and managers interests could be aligned by large shareholders or block-holders as they have incentive to discipline and monitors the actions of managers. Finally the RMS has insignificant relation with agency cost. Prior literature predicted higher directors' remunerations could reduce the agency cost because remuneration as directors' incentive will make sure the managers to act on in the best interests of the shareholders and company. However, Darren Henry (2006) reported in their research that remuneration is worked as agency problems reduction.

4.3.2 FE Regression Based on LEVJ

Table 6 shows the regression outcomes using the fixed effect model where LEVJ is depend variable and INSI is explanatory variable along with other 3 control variable like the table 4 results. Coefficient of INSI variable shows the considerably negative relation to the LEVJ with the 1% significant level. It shows that increasing in INSI will strike to decreasing of LEVJ which mean that the role of LEVJ could be substitute for INSI under the agency theory framework in order to controlling agency conflicts and the results are consistent with our economic theory. Whereas, Sorensen and Kim (1986) planted the ownership dilution theory which is supported by the similar results, that is, managers of firms carrying the higher insider ownership struggle to bypass diluting their power and control by adding debt. Mande (2010) proposed the negative insignificant relation between LEVJ and dividend of Malaysian firms. Along with LEVJ, Monde argued dividend would also help to resolve agency conflicts and misusage of free cash flows.

Coefficients of profitability representing the negative and significance relation with leverage. This is means that amount of debt will be reduced by higher profitable firms to finance its projects, since internally generated funds are available. High profitable firms incline to use of funds that are source of internally generated over externally generated like equity and debt, proposed by Majluf and Myers (1984).

Furthermore, coefficient's result of INV is consistent with our theory at 1% significance level which shows the positive relation between LEVJ and INV. This control variable is also supported by the pecking order capital structure. Leverage policy effected by firm's investing activities. Funds that are internally generated exhausted, firms to finance its projects and operations tend to external source of funds. Hence, an increment in

financial activities will push firms to debt than equity as external financing source (Majluf & Myers, 1984) documented it in analysis of pecking order capital structure.

Finally, the result of our other control variable, i.e. DDND showing the inconsistent results than our proposed theory which is positive relation between ddnd and levej. Whereas, Rozeoff (1985) argued Agency conflicts could be reduce by making higher dividends payments, in addition to that, he finds the empirical negative relationship between leverage and dividend.

Furthermore, both models as a whole are significant in explaining dependent variables' variation. R-square for AGNC model is 0.645 which means that the four explanatory variables explain 65%% variation in the response variable which is agency cost. In addition, R-square for LEVJ model is 0.837, which indicating 84% variation in the financial leverage explained by four explanatory variables.

5. Conclusion

In this study we provide the rebalancing the corporate governance which taking the stress out with substitute mechanism and indifference theory. We proof the rational that we are indifferent either using financial leverage or insider ownership to control the agency cost. Results shows that increasing in INSI will strike to decreasing of LEVJ which mean that the role of LEVJ could be substitute for INSI under the agency theory framework in order to controlling agency conflicts and the results are consistent with our economic theory.

Furthermore, the regression outcomes reporting the highly significant negative relation between sampled firms' agency cost and leverage which is supported by numerous theories and consistent with the hypothesis. First, adding debt increased the monitoring of management, i.e. banks, and to put pressure to run firms profitable. Second, debt crate the risk of bankruptcy risk and threaten the managers' job lost which considerably helps to align the managers and shareholders business interests. Finally, INSI displayed the negative relation with AGNC is significant at 5% which is consistent with ours hypothesis of agency cost mitigation through insider equity ownership and proofing the theory of Jenson Meckling.

Moreover, study's objective is to provide some fruitful and innovative guidelines for the effective mechanism of corporate governance to hedge stockholders interests, instills their confidence and to look into the long term value creation of firms. Furthermore, this is expected to contribute meaningfully in the literature of corporate finance in general and particularly for regularity bodies.

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