A PROJECT REPORT ON

Pondicherry University

DIVIDEND POLICY AND FINANCIAL PERFORMANCE OF COMPANIES

Partial fulfillment of the award of the Degree

Of

MASTERS OF COMMERCE (ACCOUNTING AND TAXATION)

Submitted By

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CERTIFICATE

This is to certify that the project entitled "**DIVIDEND POLICY AND FINANCIAL PERFORMANCE OF COMPANIES**'' submitted to the Pondicherry University in partial fulfilment of the requirement for the award of the degree of Master of Commerce (Accounting and Taxation)is a record of original project work done by **MUBASHIRA (Reg. No. 21311045)** in the Department of Commerce, Pondicherry University, under my supervision and guidance and that the project has not formed the basis before for any degree/ diploma/fellowship or any other similar titles and it represents an independent work done by the candidate.

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DECLARATION

I hereby declare that the project entitled "**DIVIDEND POLICY AND FINANCIAL PERFORMANCE OF COMPANIES**" submitted to the Pondicherry University in partial fulfilment of the requirement for the award of the degree of "Master of Commerce (Accounting and Taxation)"is a record of original project work done by me in the department of commerce, Pondicherry University, under the supervision and guidance of **Dr. SHIJIN.S** and that the project has not formed the basis before for any degree/ diploma/fellowship or any other similar titles.

Place: Pondicherry
Date:

MUBASHIRA

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MUBASHIRA

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INTRODUCTION

1.1. CHAPTER SUMMARY

Study entitled "Dividend policy and Financial Performance of Companies" begins with the 'Introduction' chapter. This chapter begins with the introduction to the main topic under study 'Dividend Policy and Companies financial performance', followed by significance of the study, scope of the study, statement of the problem, objectives of the study, hypothesis framed based on objectives, research methodology, variables used for the study and limitations of the study.

1.2. INTRODUCTION

The financial markets are considered a pivotal and important component and represent the main means of communication between corporations and accounting information users. Investors that mobilize savings and convert them into investments contribute to economic development. This provides a solid base for the economy. Recent changes in the economics and financial field have led companies to search for ways and methods that enable them to continue to achieve acceptable levels of performance, especially financial performance, and many researchers have studied the financial decisions that aim to maximize a corporation's value, not only the distribution of profits to owners (shareholders) but also the precarious conditions experienced by corporations which lead to more difficulty in decision making which may have a significant impact on company performance and company financial performance.

The income of a firm is can be put into use by paying debts, acquiring securities, investing in operating assets and/or distributing to shareholders also known as dividends. There are a number of reasons whether a firm ought to pay or should not pay dividends. Dividends are important to the investors because they are a source of current income to the investor, it is helpful in maintaining shares market price and providing a clear certainty about the financial status of a company. Increased dividend payouts positively affect companies. Companies with a history of stable dividend payout are negatively impacted by lowering dividend distribution. Declaring new dividends is perceived favourable in comparison to not having any form of dividends (Gill, Biger & Tibrewala, 2010).

Amidu and Abor (2006) observe that there are a number of reasons whether a firm ought pay or should not pay dividends, however on the other hands the Dividend Irrelevance Theory was developed by Miller and Modigliani which posits that in perfect capital markets dividend payout does not affect the value of a company, hence irrelevant. Dividend policy plays a crucial role since it decides the funds to be retained for investment by a company and the amount of funds paid to the shareholders as dividends (Ross, Westerfield & Jaffe, 2002). It also shows the stakeholders the firm's performance. Firm investments determine the future earning and potential dividends and affect cost of capital (Swee, Zakaria & Hui, 2007).

Dividend policy is described as the policy used by a company to structure shareholders dividend payout. The indicators of dividend policy are dividend yield; this is the ratio of a company's annual dividend to its share price. Dividend yield is also referred to as the estimate dividend- only return of a stock investment. With the assumption that dividend neither raises or lowers, the yield will increase with a fall in stock price, and decrease with a rise in stock price. Since dividend yield is affected with stock prices, when stocks are falling quickly, it will look unusually high. Earnings per Share (EPS) is the portion of profit of a company allocated to each common stock share that is outstanding, showing the financial status of a company. EPS is the net income of a company that can earn per share if and when the shareholders are paid all the profits. In addition, EPS is used to show the financial performance of a company and is considered a determinant of stock value.

Charumathi (2012) posits that the ration of dividend payout of a company gives investors an idea of the funds returned to shareholders in comparison to the funds used by a company for reinvestment, to pay off debt, or to add cash reserves. The figures at the bottom of a financial statement of a company are easily used to calculate the ratios. This is different to dividend yield which makes the comparison on dividend payment to the current company's stock price.

1.3. SIGNIFICANCE OF THE STUDY

A dividend is a distribution of profits by a corporation to its shareholders. When a corporation earns a profit or surplus, it is able to pay a proportion of the profit as a dividend to shareholders. The remaining profit after dividend, namely retained earnings will be used to re-invest in the future.

A high dividend payment means that the company is reinvesting less money back into its business. On the contrary, companies with low dividend payment means that the companies is reinvesting in business growth, so that the higher future capital gains for investors.

The effect of dividend policy on financial performance has been widely researched with different opinions. Some theorists strongly believe that the payment of dividends increases the values of the firms involved; others however believe that increased dividend payouts don't have any significant effect on the financial performance of the business entities. According to Gordon and Lintner (1963), the payment of high dividends will reduce risks and this has a direct effect on the financial performance. Conversely, Litzenberger (1980) argued that low dividend payouts attract reduced taxes which influence financial performance.

1.4. SCOPE OF THE STUDY

This study aims to determine the nature of the association between dividend policy and a corporation's financial performance in emerging countries, as well as the main variables that may have an effect on financial performance. The scope of study is limited to 35 companies included in Nifty 50 of National Stock Exchange. This study helps to assess the relation between Dividend policy and Financial performance of companies for financial years from 2011 to 2022.

1.5. STATEMENT OF THE PROBLEM

The research problem is embodied in the following main questions:

- Does the dividend policy affect the financial performance of companies listed in National Stock Exchange?
- Is it positive or negative or is there no impact on performance?

This study "Dividend policy and Financial Performance of Companies" is highly relevant in finding out answers for above listed questions.

1.6. OBJECTIVES OF THE STUDY

- To determine the influence of dividend yield on financial performance of companies listed in the National Stock Exchange
- To measure the impact of dividends on performance in emerging countries
- To identify the factors which are significantly contribute to the Dividend Policy Ratios and Firm Performance

1.7 Limitations of the study

The limitations of the study are;

- The study focuses only on financial items from the balance sheet, profit and loss account, and major financial ratios whereas other accounts such as notes to accounts and other parts of financial statement asides are left out.

- Sample size industries where limited to 35 companies in Nifty 50 where others are ignored.
- Since the study is mostly based on the secondary data, the shortcomings of the use of secondary data are inevitable.

1.8 RESEARCH METHODOLOGY

The broad objective of this study is to find the relationship between dividend policy and financial performance of the companies. The basic nature of this study is descriptive. This research is based on secondary data.

1.8.1 Data Source

Financial data extracted from published database of CMIE for the financial years from 2011 of 35 companies included in the Nifty 50. The datas are extracted by ProwessIQ which is a powerful internet-based application for querying CMIE's database on performance of listed and unlisted companies. The companies included are:

S.No	Name of the Company
1	Adani Enterprises Ltd.
2	Adani Ports & Special Economic Zone Ltd.
3	Apollo Hospitals Enterprise Ltd.
4	Asian Paints Ltd.
5	Bajaj Auto Ltd.
6	Bharat Petroleum Corpn. Ltd.
7	Britannia Industries Ltd.
8	Cipla Ltd.
9	Coal India Ltd.
10	Divi's Laboratories Ltd.
11	Dr. Reddy's Laboratories Ltd.
12	Grasim Industries Ltd.
13	H C L Technologies Ltd.
14	Hero Motocorp Ltd.
15	Hindalco Industries Ltd.
16	Hindustan Unilever Ltd.
17	I T C Ltd.

18	Infosys Ltd.
19	J S W Steel Ltd.
20	Larsen & Toubro Ltd.
21	Mahindra & Mahindra Ltd.
22	Maruti Suzuki India Ltd.
23	N T P C Ltd.
24	Oil & Natural Gas Corpn. Ltd.
25	Power Grid Corpn. Of India Ltd.
26	Reliance Industries Ltd.
27	Sun Pharmaceutical Inds. Ltd.
28	Tata Consultancy Services Ltd.
29	Tata Consumer Products Ltd.
30	Tata Steel Ltd.
31	Tech Mahindra Ltd.
32	Titan Company Ltd.
33	U P L Ltd.
34	Ultratech Cement Ltd.
35	Wipro Ltd.

1.8.2 Periodicity

As regard use of statistical data for analyses, the study contains a period of eleven financial years, i.e., from 2011 and 2021.

1.8.3 Sampling design

The sample of this study composed of 35 Companies listed in Nifty 50 of National Stock Exchange.

1.8.4 Analysis tools used

The study used Panel Data Analysis and cross-sectional time-series data and multiple linear regression models. A multiple regression model was also developed in order to test whether guess factors may have a possible impact on financial performance (such as Dividend Yield, Firm Size, Leverage Ratio, Current Ratio).

1.9 CHAPTERISATION

I. INTRODUCTION

II. REVIEW OF LITERATURE

III. DIVIDEND POLICY

IV. FINANCIAL PERFORMANCE BASED ON DIVIDEND POLICY

V. CONCLUSIONS

CHAPTER 2

REVIEW OF LITERATURE

2.1. CHAPTER SUMMARY

A literature review is a comprehensive summary of previous research on a topic. The literature review surveys scholarly articles, books and other sources relevant to a particular area of research. Literature reviews are a basis for research in nearly every academic field. The literature review acknowledges the work of previous researchers and in so doing, assures the reader that your work has been well conceived. It is assumed that by mentioning a previous work in the field of study, that the author has read, evaluated and assimilated that work into the work at hand.

A literature review creates a "landscape" for the reader, giving her or him a full understanding of the developments in the field. This landscape informs the reader that the author has indeed assimilated all previous, significant works in the field into his or her research.

The main objective behind this chapter is to covey the reader what knowledge and idea have been established on a topic, and what their strengths and weakness are. The main purpose of literature review is to provide foundation of knowledge on topic, identify areas of prior scholarship to prevent duplication and give credit to other researchers.

The present chapter deals with latest literature reviews made in the field of financial Dividend policy and Financial performance.

2.2. REVIEW OF LITURATURE

- **Juma'h and Pacheco (2008)** did a study on the financial factors influencing cash dividend policy: a sample of U.S. manufacturing companies. Some of the factors considered in this study included profitability ratios, liquidity ratios, expansion and investment, investors' perceptions, companies risk, and companies' size. A regression model was used. The research findings confirmed that profitability, liquidity, risk and company size on average, are important determinants of cash dividend decision.

- **Anand (2004)** sought to find out the determinants of the dividend policy decisions of the corporate India. The findings established that most of the firms have target dividend payout ratio and dividend changes follow shift in the long-term sustainable earnings. The dividend policy therefore, is designed after taking into consideration the investors' preference for dividends and clientele effect. The study also found that dividend policy is used as a signaling mechanism to convey information on the present and future prospects of the firm and thus affects its market value. Mohanty's (1999) survey of the dividend payout ratio of the Indian companies indicate that firms maintain a constant dividends per share and have fluctuating payout ratio depending on their profits.

- **Mancinelli and Oskan (2006)** and Mohammed et al (2011) who also had similar study on the dividend payout and corporate performance in Italy and Ghana respectively. The result of both study showed a significant relationship between the variables of study.

- **Lee (2009) of Kenya and Huda and Farah (2011) of Bangladesh, Marfo-Yladom and Agyei (2011)** of Ghana also had similar study on the banking industry as the outcome of their study identify not only significant relationship between dividend payout and profitability but also include other economy variables: leverages, changes in dividend, growth and age of firms and many factors that are responsible for dividend payout.

- **Nikolaous (2005)** examined the effect of distributed earnings and size of the firm to its dividend policy using Greek data at the conclusion that Greek companies prefer to distribute, each year a rather constant dividend, which they adjust from year to year according to their distributed earnings and size.

- **James (2014)** who reviewed the work of Aloizieuwa (1974), Inanga (1975, 1978), Soyode (1975) and Oyejide (1976) examined the dividend policy and profitability in the banking industry, agreed that there is no doubt on the correlation between the dividend policy and profitability and growth. Stephen et al (2015) also examined the impact of dividend policy on the share price valuation in Nigeria concluded that dividend policy has a positive effect on shareholders' wealth. Olatundun (2003) also studied on similar topic had an empirical results that there is relationship between cash flows and dividend changes depend sustainability on the level of growth, the capital structure choice, size of each firm and economic policy changes. Olowe et al (2014) using regression analysis to study the subject matter concluded that the result obtained are in line with previous studies and support the view that banking risks negatively influence dividend payout.

- **Aivazian and Cleary (2003)** maintain that firms are more likely to raise their dividends if they are large and profitable. Nissim and Ziv (2001) also agree that dividend increases are associated with future profitability while dividend decreases are not related to future profitability. Amidu (2007) also found that dividend policy affects firm performance especially profitability. The results showed a statistically positive and significant relationship between profitability and dividend payout. Therefore, just like the dividend preference theory, investors expect a dividend increase with an increase in profits.

- **Lubis et al. (2017)** and Imelda and Sheila (2018) found that the current ratio had a significant positive effect; the debt to equity ratio has a significant negative effect; total assets turnover has a significant positive effect; ROE does not affect firm value. Assets turnover and ROE have a significant effect on firm value. Research conducted by Pertiwi (2016) shows that profitability is not significantly positive effect; dividend policy is not a significant positive effect; profitability has a positive and significant effect on dividend policy, but the Dividend policy is not able to mediate the relationship between the effect of profitability with firm value. Meanwhile, based on the results of Farooq's research (2016), the results show that leverage has a significant and positive effect on firm value, and firm value effect on firm size, negatively.

- **Alii, Khan, and Ramirez, (1993)** Examined that the relationship between expected price-to-book ratio, dividend per share, dividend payout ratio, systematic and unsystematic risks. The sample includes the non-financial firms in the DJIA, the period 1997-2006. The result show, the variations in price-to-book ratios, systematic and unsystematic risks are not due to dividends per share. Then, the relationships between expected price-to-book ratio and dividend payout ratios are intrinsically nonlinear. Finally, the expected dividend payout ratios can be used efficiently for signaling purposes as well as a proxy for measuring the agency problem.

- **Uwalomwa, Jimoh and Anijesushola (2012**) investigated the relationship between the financial performance and dividend payout among listed firms' in Nigeria. Variables are ownership structure, size of firms and the dividend payouts. The period2006-2010 was utilized as the main source of data collection for the 50 sampled firms. Find out that there is a significant positive association between the performances of firms and the dividend payout of the sampled firms in Nigeria. Additionally revealed that ownership structure and firm's size has a significant impact of the dividend payout of firms too.

- **Samuel Kwaku Agyei, Edward Marfo-Yiadom (2011)** examined the relationship between dividend policy and performance of banks in Ghana. The study used panel data constructed from the financial statements of 16 commercial banks in Ghana for a period of 5 years, from 1999-2003. These financial statements were obtained from the Banking Supervision department of Bank of Ghana. STATA was used for the data analysis. Indicate that banks pay dividend increase their performance. Generally, the result is shown that dividend policy has an effect on firm value.

- **Timothy Mahalang'ang'a Murekefu Ochuodho Peter Ouma** revealed that establish the relationship between dividend payout and firm performance among listed firms in the Nairobi Securities Exchange. Regression analysis was carried out to establish the relationship there. This study made use of both primary and secondary data. Secondary data was obtained from the firm's annual reports, from the year 2002 to 2010. The population for this study consisted of the firms listed on the Nairobi Securities Exchange. The NSE classified these companies into ten sectors. The findings indicated that dividend payout was a major factor affecting firm performance. Their relationship was also strong and positive. Based on the findings of this research that dividend policy is relevant and that managers should devote adequate time in designing a dividend policy that will enhance firm performance and therefore shareholder value.

- **Arnott & Asness (2003)** pointed the positive relationship between dividend payout and growth in future earnings is that managers are reluctant to cut dividends. A high payout ratio indicates management's confidence in the stability and growth of future earnings and a low payout ratio suggests that management is not confident of the stability of earnings or sustainability of earnings growth (Arnott & Asness, 2003). Managers therefore pay low dividends to avoid dividend cuts when earnings drop.

- **Ghana Stock Exchange, Amidu (2007)** found that dividend policy affects firm performance especially the profitability measured by the return on assets. The results showed a positive and significant relationship between return on assets, return on equity, growth in sales and dividend policy. This showed that when a firm has a policy to pay dividends, its profitability is influenced. The results also showed a statistically significant relationship between profitability and dividend payout ratio.

DIVIDEND POLICY

3.1. CHAPTER SUMMARY

The theoretical framework is the structure that can hold or support a theory of a research study. The theoretical framework introduces and describes the theory that explains why the research problem under study exists. Through this chapter various concepts related to financial literacy and personal financial decisions have been discussed.

Strong conceptual frameworks capture something real. Conceptual frameworks are particularly useful as organizing devices in empirical research. One set of scholars has applied the notion of conceptual framework to deductive, empirical research at the micro or individual study level.

The theoretical framework plays an important role in guiding the entire process of the study. Theories are constructed in order to explain, predict and master phenomena. It helps the researcher see clearly the variables of the study. A conceptual framework is used in research to outline possible courses of action or to present a preferred approach to an idea or thought.

The present chapter deals with important theories associated with Dividend policy and Companies financial performance.

3.2 Dividend Policy

Dividend policy means how much cash is distributed to shareholders. Dividend policy can be determined through two important elements, the first is the decision to pay dividends to shareholders and the second is to retain the profits to reinvest them in future projects. The company is responsible for balancing the need to maximise the wealth of the company's owners with the need to provide sufficient funds to finance growth projects, which is a major role that acts as a mechanism to control administrative opportunism. Companies carry out many activities through which they seek to achieve profits. A corporation finds itself with two options for the funds that it obtains, to either distribute part of the profit to investors (dividends) or keep a portion of the profit to reinvest later for the purposes of expansion and growth, taking into account that the decision to distribute the profits is of great importance to the owners, there is a missing link between distribution and growth, and the policy of dividend distribution can be determined through balancing the level of distribution and the rate of growth. Since growth is one of the components of the distribution model, the issue of distributions is considered on the basis of choosing between current cash distributions after an evaluation of the company's current situation and its ability to exploit the profits in the expansion projects and opportunities for growth.

The decision to distribute dividends is one of the powers of the Board of Directors, which is affected by sums of factors. The most important factors for controlling distribution proportions include the corporation's financial ability, its aspirations for the future and the wishes of investors. The amount of distributions is an important matter for both the corporation and its investors; thus, there are a set of factors that can influence dividend policies:

3.2.1 Legal Legislation*:* Legal rules and legislation are differentiated among countries and affect profit distribution policy, usually based on four main rules: net profit rule, weak capital rule, the insolvency rule and the tax penalty rule. These rules are considered binding restrictions for institutions when setting the framework for dividend policy.

3.2.2 Profitable Investment Opportunities*:* If the institution does not have any profitable investment opportunities, it distributes profits to its shareholders. But if the institution has profitable investment opportunities, it will resort to using the profits achieved to fund those opportunities.

3.2.3 Current Shareholders' Needs (Preferences): The preferences of the current shareholders are considered one
of the most important determinants of the dividend policy. In institutions in which ownership is limited to a small number of individuals, there is a clear trend towards capturing a high percentage of profits and distributing a small percentage to shareholders, as the current shareholders prefer to secure the company's financing needs through these profits (retained earnings) rather than through the issuance of new shares. The issuance of new shares leads to the entry of new shareholders, and current shareholders do not want to lose control or borrow until they bear the expenses (interest) of the loans.

3.2.4 Availability of Cash Liquidity*:* This is considered an important indicator because the distributed profits represent external cash flows. Therefore, the better an institution's position in terms of liquidity, the greater its ability to pay dividends.

3.2.5 Growth and Expansion Projects*:* An institution that is going through a growth stage will need to have financial resources available to fund growth projects. Reliance on self-financing sources may be better than resorting to external financing sources (borrowing), and this calls for institutions to retain profits because this will save the interest expense that results from borrowing.

3.2.6 Factors Relating to Owners and Capital Markets*:*

Dividend policy is affected by the owners' wants and needs. In addition, it is affected by the capital markets through the adoption of a low dividend pay-out ratio.

3.3. Theories Explaining the Dividend Policy

Dividend policy is considered an important strategic financial decision and it is subject to several considerations in its determination. There are many theories that try to explain the behaviour of investors towards the dividend policy, and these theories differ between supportive and neutral towards the impact of the dividend distribution policy on company financial performance. The most important of the theories that have attempted to explain distribution policy are:

3.3.1. Neutral Theory (Dividend Policy)

The credit for discovering this theory goes to two economists M&M (Modigliani & Miller, 1961). According

to this theory, the profit distribution decision has no effect on the stock price in the market or the market value of the corporation. Instead, corporation value is affected only by the profits achieved and the risks to which the corporation's assets or investments could be exposed. Thus, the corporation's market value is affected only by the income generated from asset management and not by how this income is divided among shareholders through cash distributions or retained earnings. These authors affirmed that investment efficiency is the main determinant of shareholder wealth; they also found that investors do not distinguish between obtaining cash through distributions or the corporation's reinvestment of its profits to achieve growth, which, in turn, leads to an increase in the wealth of owners. They further said that the concept of capital gains is based on increasing the market price of shares that are held before declaring dividend distributions; if the corporation has achieved profits and decided to distribute part of it, the market value of the shares will decrease by the amount of the dividends, and if the corporation has decided to retain the profits as retained earnings, the market value of the shares will increase by the amount of retained earnings. This theory's validity does not match reality as determined from (M&M), so their theory is unrealistic and needs more investigation or scientific testing.

3.3.2. Bird-In-The-Hand Theory

This theory developed by Gordon and Litner is attributed to the first theory, namely, the neutral theory of dividend policy, which stated that there is no relation between the profit distribution policy and the stock price or corporation value. It resulted as a criticism of previous theory (M&M theory). This theory indicates that the dividend policy has a direct impact on the market value of the corporation through its effect on the market share price because the required rate of return on the funds owned decreases with the increase in dividends. This

is due to the fact that the degree of investor certainty about the obtainment of capital gains realised from the retained earnings is less than the degree of certainty obtained from the capitalization of dividends, as the degree of risk increases as a result of the high uncertainty from retaining profits and reinvesting them. This means that investors prefer to distribute profits over achieving capital gains in the future, since the profits distributed today are more certain than the possibility of obtaining future capital gains.

3.3.3. Tax Preference Theory

According to this theory, if capital gains related to the sale of shares are not subject to tax, or if the tax rate on these profits is less than the tax rate on cash dividends distributed, investors prefer that corporations do not distribute cash dividends but retain profits in the form of profits undistributed. The lower the percentage of cash dividends at the expense of undistributed profits, the higher the shareholders' wealth, with other factors remaining constant.

Investors will therefore demand that corporations distribute large amounts of cash dividends with greater returns than they accept from other corporations. Thus, corporations distribute cash dividends in order to compensate for the amount of taxes that investors will pay.

3.3.4. Signal Theory

This theory states that managers use the payment of dividends as a signal to communicate private information about the corporation to external investors and shareholders about the prospect for profits and their successful performance (excellent management). Therefore, a higher distribution will give a signal to investors that the corporation's prediction of future earnings is positive; in other words, if the distribution was less than the dividend – but paying with a higher percentage – investors expect the company value to rise and if the investors expected a high percentage of the dividends, while the corporation paid a much lower percentage, the price of the shares will drop in the financial market.

3.3.5. Clientele Effect Theory

This theory suggests that due to the changes in dividend policies, investors always make decisions depending on
the dividend polices chosen by firms which may encourage investors to continue with this firm or transfer to another firm.

3.3.6 Agency Theory

According to this theory, investors want to increase their cash gains by the distribution of a greater percentage of
profits, while management prefers to increase the portion of retained earnings to ensure the availability of enough funds for investment or expansion purposes, leading to agency conflict.

3.4 Dividend Forms

There are many ways to distribute profits to shareholders; among them, we find the following:

3.4.1 Stable Dividend Policy

This mechanism includes the process of distributing profits on a regular basis (fixed rate), thus satisfying the shareholders wants and overcoming the problems of fluctuation in profits by always paying minimum dividends every year.

3.4.2 Progressive Dividend Policy

This represents the process of distributing dividends in line with the realised profits and increasing the earnings per share.

3.4.3 Regular Dividend Policy

In accordance with this policy, regular profits are distributed to all shareholders every year. In the event that the profits are large and unnatural, these profits are kept in retained earnings and the excess profits will not be distributed to the shareholders.

3.4.4 Irregular Dividend Policy

This mechanism uses the policy of distributing profits in an irregular manner. Companies always resort to this mechanism when there is no fixed level or stability in profits or no continuity in achieving profits or the company does not have sufficient liquidity.

3.4.5 Scrip Dividends

These dividends are always known as liability profits and are distributed to shareholders in the form of a certificate instead of cash dividends. They provide an option for the shareholders to obtain profits at a later time or to obtain additional shares. Companies issue such profits when they don’t have sufficient cash to pay cash dividends.

3.4.6 Non-Cash Dividends

In this policy, corporations resort to distributing new shares to shareholders instead of paying cash dividends. This procedure requires the corporation to possess reserves and profits that are heavily withheld (retained earnings) along with a desire to retain earnings and reserves to future periods based on promising investment opportunities. Fundamentally, however, the negative effect of this policy is the decrease in the share market value, so corporations resort to this policy when the stock’s market value increases significantly, but a decrease is feared in the number of investors wishing to buy shares. Also, this type of distribution is characterized by not being taxed, and this process adjusts the ownership of shareholders, so that each shareholder has a greater proportion from dividends without making any changes to shareholder wealth.

3.4.7 Shares Split

This policy is another alternative to the distribution of cash.This technique could be defined as the procedure which results in additional shares and leads to an increase in the number of shares by reducing the nominal value of the stock, usually used to create demand for shares by increasing the number of shares in the capital of the corporation. This process leads to a decrease in the dividend per share when the amount of the dividends is fixed or to the stability of the dividends per share with an increase in the amount of the total dividends. It should be noted that there is a similarity between the derivation of shares anddistributions of shares in financial terms.

3.4.8 Share Buybacks (Reverse Stock Splits)

This policy is the inverse of the derivation of the number of its shares. As appears from its name, this policy is based on the same principle of the derivation process of shares but in an inverse way which leads to raising the nominal value of the share. Therefore, there is no change in the financial structure of the corporation except for the number of shares. The reverse derivation method is a policy to prevent the stock price from falling to low levels. Stock repurchase (treasury shares), as the corporation's buyback of its shares, is intended to use the surplus of cash in the corporation to buy its traded shares, which are called treasury shares. This policy thus leads to the creation of so-called shares cash and stock prices are mostly greater than the price prevailing in the market.

There is another method, which is called the repurchasing of the target shares through management corporation practices, such as negotiating with shareholders who have large proportions of shares, to thwart control over the corporation's shares. Corporations usually negotiate with some investors to the Foundation when the market share price is less than its true value. The stock repurchase policy has witnessed staggering growth in the United States and Europe.

3.4.9 Quality Distributions and Bond Dividends

This policy is also called distributions of quality in which the management of the corporation makes distributions of goods, real estate, investments or bonds in place of cash distributions. Corporations resort to this type of distribution when they have liquidity problems (the lack of necessary liquidity), but this type of distribution is not desired by shareholders as cash dividend distributions allow greater freedom for contributors to meet their needs and wants.

FINANCIAL PERFORMANCE BASED ON DIVIDEND POLICY

4.1 CHAPTER SUMMARY

Data analysis and interpretation is the process of assigning meaning to the collected information and determining the conclusions, significance and implications of the findings. Secondary data of 35 companies in Nifty 50 have been analyzed through E-views. The study used Panel Data Analysis and cross-sectional time-series data and simple and multiple linear regression models. A multiple regression model was also developed in order to test whether guess factors may have a possible impact on financial performance (such as Dividend Yield, Firm Size, Leverage Ratio, Current Ratio). Based on the objectives framed; 2 hypotheses formulated for the study have been tested and presented in this chapter.

4.2 Study Variables and Hypothesis Development

The independent variable included in the study (dividend policy) was measured through dividend yield, consistent with Anandasayanan and Thirunavukkarasu (2016), Farrukh et al. (2017) and Widiyanti et al. (2019) Dividend yield represents the sum of the annual distributions that a corporation pays to its shareholders on their investments. At the same time, it shows investment attractiveness in a corporation's shares. Dividend yield could also be represented by ROI for investors who do not prefer capital gains or long-term earnings. It is calculated as 'annual dividend per share' divided by current market value per share': Dividend Yield=Dividends Per Share/Market Stock Price. It measures the investor return that may be made from dividends alone which becomes part of the expected return on investment.

Financial performance usually focuses on revenue and profit margins, and one of the key profit-based metrics is the 'net profit' measure. Net profit is calculated as an amount that must be converted into a proportion of revenue; that is, net profit margin For example, if the benchmark net profit margin for a particular industry is 40%, the new company in the industry must work to reach or exceed this number (40%) in order to compete. A 'gross profit margin' is a common measure of performance based on profit that measures revenue after deducting the expenses directly related to the production of goods. There are special standards for each department that are not suitable for another department, known as the criteria for measuring and evaluating performance. Financial indicators are used to evaluate the company's performance, as the company's success depends on achieving revenue and the effective management of financial resources. Shareholders, investors and customers use financial data to evaluate the company's performance as well as its ability to grow and achieve profit, cost measurement, comparison of the proposed budget with the actual budget and other financial indicators to assess company health and profitability. There are many measures used in the literature to assess financial performance (Hindasah & Nuryakin, 2020). The discussion that follows will highlight the means that are most used for this purpose: liquidity ratios. These ratios are used to measure the ability of the enterprise to meet short-term obligations.

4.2.1 Activity or asset management ratios*:* These indicate the efficiency of management in using assets to generate returns. There are a number of indicators used to measure the activity, which are: stock turnover, sale period, collection period, turnover of capital, turnover of fixed assets and turnover of total assets (assets).

4.2.2 Leverage ratios or debt management*:* This refers to the degree of financing the company has established through debt. The success of using finance by means of debt rather than owner financing means management has the ability to increase the return to shareholders. The indicators used for these ratios are total debt to total assets and the ratio of indebtedness to total financial capital.

4.2.3 Profitability ratios*:* These assess the efficiency and effectiveness of an enterprise in generating profits; if the enterprise does not obtain sufficient profit then its long term survival will be threatened. The indicators used to measure these ratios are net profit margin on sales, return on
investment, return on equity and earnings per share.

4.2.4 Evaluation ratios*:* These ratios aim to raise the market value of the enterprise's shares. The enterprise's share prices are related to the book value of one share. These ratios have a number of indicators, including share price to share per ordinary share and the market value of the share to the book value.

4.2.5 Growth rate*:* The growth period of the institution is measured in the framework of the growth of the national economy, represented by the growth of national income or gross national product or the growth of the sector in which the company operates. The indicators used are net sales growth, net income growth, profit growth per ordinary share and growth dividends divided by one ordinary share. The current study will apply the most important factors to measure financial performance through the use of profitability indicators (ROA and ROE), consistent with Freihat and Kanakriyah (2017); Ali et al. (2020).

4.3 The random error*:* This error is likely to exist for several different reasons, including those related to neglecting some independent variables that can affect the dependent variable, incorrect mathematical formulation of the model or the result of an error in both the collection of some data and the measurement of financial variables.

4.4 Statistical methods and tools used*:* This study relied on simple and multiple linear regression methods for testing and proving the validity of the study hypotheses when (α <0.05) with degree of confidence (95%), and for this reason applied the following tests to ensure achieving the study's purposes: regression analysis, correlation (correlation matrix) and descriptive statistics.

This study seeks to test the following hypotheses:

H1: *There is a strong association between dividend policy and return on assets.*

H2: *There is a strong association between dividend policy and return on equity*

Dividend policy is measured by dividend yield along with other control variables as mentioned before.

4.5 Control Variables

Control variables that were employed in the current study include firm size because large firms have the ability to pay more dividends (Phornlaphatrachakorn & Khajit, 2020) (the firm size will be measured through the natural logarithm of total assets); the current ratio; and the leverage ratio. Current ratio represents current assets divided by current liabilities. While the leverage ratio shows the volume of external financing from short-term and long-term debts, creditors prefer low rates of savings because the lower the percentage, the higher the margin of safety, which means creditors can recover their dues in case of liquidation. This ratio is measured through total debts divided by total assets. To test the impact of dividend policy on financial performance, the study will test the effect of dividend policy on ROA and ROE for eleven years (2011-2021). The variable used as a proxy to measure the financial performance is return on assets (ROA) and return on equity (ROE) through applied pooled regression as detailed in the equation below.

$$ROA = \beta 0 + \beta 1\ DY + \beta 3\ CRA + \beta 4\ LRA + \beta 5\ FSIZE \quad (1)$$

$$ROE = \beta 0 + \beta 1\ DY + \beta 3\ CRA + \beta 4\ LRA + \beta 5\ FSIZE \quad (2)$$

Where:

ROA, ROE: Used as a proxy for Financial Performance

DY: Dividend Yield

CRA: Current Ratio.

LRA: Leverage Ratio.

FSIZE: Firm Size.

$\beta 0$: Intercept

Table 4.6: Study Variables and Methods to Measure Them

Variable	Type	Code	Proxies
Return on Assets	Dependent	ROA	Proxy to measure financial performance
Return on Equity	Dependent	ROE	Proxy for measure financial performance
Dividend Yield	Independent	DY	Dividend Yield = Dividends per share / Stock price
Current Ratio	Independent	CRA	Measured by current assets divided by current liabilities
Leverage Ratio	Independent	LRA	Measured through total debts divided by total assets
Firm Size	Independent	FSIZE	The natural logarithm of the total assets

4.7 Descriptive Statistics

Table 4.7.1 shows the ROA and ROE indicators used to measure performance for the companies that were surveyed.

Table 4.7.1 Descriptive statistics

	CRA	DY	FSIZE	LRA	ROA	ROE
Mean	1.822829	0.023296	12.65847	0.946728	11.91709	21.9766
Maximum	7.430331	0.2902	16.08982	5.649118	77.5753	142.01
Minimum	0.263153	0.0005	9.622371	0.132065	-19.3075	-38.18
Std. Dev.	1.148807	0.040196	1.248083	0.979186	10.62473	19.26193
Observations	385	385	385	385	385	385

Return on assets shows excellent profitability which reached to 77.6% with standard deviation (SD) 10.6. ROA shows the ability of the funds invested in the company to achieve net profit, with full coverage of operating and non-operating costs. The ROE values are between the range of -38.18 and 142.152. It also shows the excellent performance of company. Debt equity ratio is taken as leverage ratio. It has reached maximum of 5.6 which is considered as risky. Dividend yield during the study period ranges between zero and up to .29 with an average of 2.3%. The current ratio for surveyed companies ranges between .26 to 7.43, which indicates companies may mismanaging or underutilizing the assets. The firm size range between 9.6–16.1 is due to the large difference in size from one company to another as a result of the difference in the size of the assets between these companies.

4.8 Empirical Tests and Analysis

This part presents the main results. The variables correlation matrix is illustrated in Table 4.8.1 below.

Table 4.8.1 Correlation result

E views correlation	CRA	DY	FSIZE	LRA	ROA	ROE
CRA	1	-0.09694	-0.22906	-0.34752	0.399552	0.145926
DY	-0.09694	1	0.26972	-0.08997	0.107236	0.087104
FSIZE	-0.22906	0.26972	1	0.036441	-0.23527	-0.30232
LRA	-0.34752	-0.08997	0.036441	1	-0.17874	0.072558
ROA	0.399552	0.107236	-0.23527	-0.17874	1	0.828378
ROE	0.145926	0.087104	-0.30232	0.072558	0.828378	1

Correlation is the determination of linear relationship between two distinct variables. The table 4.8.1 shows that variables Return on asset and Return on equity have high positive correlation (.83).

Multiple regression is used to analyze the relationship between a single dependent and several independent variables.

The first equation

$ROA = \beta0 + \beta1\ DY + \beta3\ CRA + \beta4\ LRA + \beta5\ FSIZE \quad (1)$

is tested here.

To make sure there is no multicollinearity problems, the VIF (variance inflation factors) test was done for which the result is shown through Table 4.8.2.

Table 4.8.2 VIF Result 1

Variable	Centered VIF
DY	1.101004
CRA	1.210864
LRA	1.15792
FSIZE	1.149302
C	NA

The results of VIF shows values were less than 10 for all variables as shown in Table 4.8.2, which means multicollinearity is not problematic.

Regression result is given below in the table 4.8.3

Table 4.8.3 Regression result 1

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DY	51.90376	12.58924	4.122865	0
CRA	3.338101	0.461947	7.226156	0
LRA	-0.304309	0.529987	-0.574181	0.5662
FSIZE	-1.765459	0.414252	-4.261796	0
C	27.42011	5.54595	4.944169	0
R-squared	0.219117			
Adjusted R-squared	0.208815			
F-statistic	21.2696			
Prob(F-statistic)	0			

Dependent Variable: ROA

The table 4.8.3 shows the panel data regression of first equation in which dependent variable is Return on assets. The probability of variables Dividend yield, Current ratio, firm size is less than .05 which shows that they are significant. The probability value of leverage ratio is more than .05 which shows that they are not significant.

When Return on Assets increases by 1% Dividend yield increases by 52% and current ratio by 3%. 21% of variation in return on assets is due to the mainly dividend yield. F statistic shows that this model is acceptable.

The independent variable displays that the following relation between dividend yield have a positive significant effect on ROA asserted through (p-value =.00 < 0.05). The results present a negative significant relation between leverage ratio and ROA.

Next the second equation

ROE = β0 + β1 DY + β3 CRA + β4 LRA+ β5 FSIZE (2)

is tested.

To make sure there were no multicollinearity problems the VIF (variance inflation factors) test was done and results are shown through the table 4.8.4.

Table 4.8.4 VIF Result 2

Variable	Centered VIF
DY	1.101004
CRA	1.210864
LRA	1.15792
FSIZE	1.149302
C	NA

The table shows the VIF factor of second regression equation. The results of VIF shows values were less than 10 for all variables as shown in Table 4.8.4, which means multicollinearity is not problematic.

The regression result of second equation is given in the table 4.8.5

Table 4.8.5 Regression result 2

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DY	98.46527	23.80851	4.135718	0
CRA	2.379618	0.873624	2.723847	0.0068
DPR	-1.014971	1.735266	-0.584908	0.559
LRA	3.001506	1.002301	2.994617	0.0029
FSIZE	-5.154221	0.783425	-6.579084	0
C	78.07271	10.48838	7.443733	0
R-squared	0.150257			
Adjusted R-squared	0.139047			
F-statistic	13.40344			
Prob(F-statistic)	0			

Dependent Variable: ROE

The regression result of second equation is given in the table 4.8.5. The probability of variables Dividend yield, Current ratio, Leverage ratio, firm size is less than .05 which shows that they are significant.

When Return on Assets increases by 1% Dividend yield increases by 98% and current ratio by 2% and leverage ratio by 2%. 14% of variation in return on equity is due to mainly dividend yield. F statistic shows that this model is acceptable.

The independent variable displays that the following relation between dividend yield have a positive significant effect on ROE asserted through (p-value =.00 < 0.05). The results present a negative significant relation between leverage ratio and ROE.

CHAPTER 5

CONCLUSION

5.1. CHAPTER SUMMARY

This final chapter deals with the conclusion. Final outcome of entire study is highlighted through this chapter.

5.2 CONCLUSION

This study aimed to test the impact of dividend policy on company performance of35 companies included in Nifty 50. In addition, the study aimed to provide valuable strategies to enable stock market participants to understand the role of dividend policy and how it can affect company performance. In this study, we tried to answer the study question (problem) that related to the effect of the dividend policy on company performance. The study founded that:

- Distribution policy does have a positive effect on the performance of companies in the National Stock Exchange during the period from 2011-2021 through the effect of dividend yield (independent variable) on the performance (dependent variable) at a significance level of 0.05
- While the results of the multiple regression test revealed that there is a significant effect of the dividends policy on the performance of the shares of the listed companies.
- Dividend yield have significant role in the financial performance.
- Current ratio influences the financial performance at moderate level.
- Leverage ratio influences the Return on equity at moderate level.
- These important results detect an influential relationship between dividend yield on one side and performance on the other side which satisfies both of the hypothesis.

This model can be used as a plan to help company managers evaluate dividend policies and will also be helpful to investors to understand management's vision. This study recommends the corporate management search for investments with high profitability as well as to benefit from external financing because it provides the necessary funds so that the company maintains a rate of growth characterized by stability which enables it to distribute cash to shareholders. Companies listed in National Stock Exchange should ensure that they have a good and robust dividend policy in place that can enhance their level of profitability and also attract investments. The board of directors of companies should be prudent in declaring dividend as higher dividend yield could mean that the share price is underpriced which could affect future dividend.

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