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EMPIRICAL INVESTIGATION ON THEORIES OF DIVIDEND POLICES-RELATION BETWEEN PAY-OUT RATIO AND FINANCIAL PERFORMANCE

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ABSTRACT

The purpose of this study is to examine the application of dividend theory in various market contexts by analyzing existing theoretical literature and empirical evidence on dividend policy. Several theories have been proposed to explain the relationship between dividend policy and firm value. Prior to the seminal paper by Modigliani and Miller in 1961, it was widely assumed that dividend policy had a significant positive influence on company value and that managers could easily influence investor behavior by changing its dividend payment policy. The determination of the appropriate dividend and retained profits mix, as well as its impact on profitability, has been a source of contention in financial management literature. This research aims to contribute to the ongoing discussion by investigating the relationship between dividend pay-out ratio and financial success. It is recommended that corporations strive to implement a strong dividend payout strategy that encourages investment in initiatives with a positive Net Present Value.

KEYWORDS- Dividend, dividend pay-out policy, profitability.

INTRODUCTION

The term "dividend" comes from the Latin "dividendum." "That which is to be distributed" is what this means. Dividends are payments made from profits to shareholders based on their percentage of ownership. Based on their percentage of ownership in the company, each shareholder of the company is entitled to a piece of the dividend. The ratio of retained to distributed earnings is referred to as the dividend choice or dividend policy. The three other decisions of investing, financing, and liquidity are all connected with the dividend decision. Companies determine the percentage of earnings to be dispersed as dividends and the percentage to be kept with the goal of maximizing shareholder wealth.

The companies should determine the ideal dividend payout with a risk-return trade-off that leads to the goal of maximizing shareholder wealth. The type and timing of dividend payments must be determined by the companies.

Pettit (1972) claimed that changes in dividend announcements cause changes in the market price of shares. Following the announcement of dividend payments, positive anomalous returns were discovered by Gordon (1959, 1962) and Vickery (1978). According to Easton and Sinclair (1989), stock prices reacted negatively to dividend announcements. After conducting an analysis, Uddin and Chowdhury (2005) concluded that dividend announcements lacked any informational value. Based on earlier research, it was discovered that the influence of dividend announcements on share price movement had been inconsistent. In this study, the effect of dividend announcement on stock market price was examined year-by-year and market capitalization-by-market-capita. This study's primary goals are to explore the effects of dividend distribution and related factors on shareholders' wealth and to determine how dividend announcements affect share prices.

Dividends continue to be one of the trickiest riddles in corporate finance, according to Allen et al. (2000), even though a variety of ideas have been proposed in the literature to explain their persistent existence.

Even Frankfurter et al. (2002) came to the conclusion that "The dividend puzzle is one of the most challenging topics of modern finance/financial economics, both as a share value enhancement and as a matter of policy." Despite forty years of research, it has remained unsolved. The goal or objective of the company has not changed over the past few decades, but the scope of financial management and the duties of a finance manager have. Maximizing shareholder wealth is the firm's primary goal. The favorable net present value of the financial decisions serves as its representation.

According to Azhagaiah & Sabaripriya (2008), shareholders believe that an increase in the company's share market price creates wealth. Even numerous researchers have established this. The value of the company is determined by each of the four financial decisions, including investment, financing, dividend, and liquidity. The production of value for shareholders is influenced by all four actions taken collectively.

One of the crucial financial choices that helps shareholders build wealth is the choice to pay a dividend. Some dividend theories support the idea that payout decisions have an impact on a company's market value, while others refute it. Those who have established a link between dividend decision and firm value frequently draw a parallel between dividend decision and investment options offered by the company.

LITERATURE REVIEW

In her 2011 study, Shaveta Gupta examined the management concerns and factors that influenced dividend decisions in the Indian engineering, FMCG, IT, and textile industries between 2004 and 2008. Shareholder wealth was calculated as the ratio of Market Value to Book Value. With the exception of the textile industry, where the dividend payout ratio was only negatively significant for the year 2006, all years and industries saw a negative correlation between dividend pay-out ratio and shareholder wealth.

Gul et al. (2012) investigated the connection between Karachi Stock Exchange's 75 companies' dividend policies and shareholders' wealth from 2005 to 2010. Market price was utilized as a proxy for shareholder wealth, and as independent variables, dividends per share, lagged price earnings per share ratios, retained earnings, and lagged market price per share were also employed. When compared to non-dividend paying corporations, the average market value to book value of equity for dividend paying companies was quite high. Through the use of multiple regression and stepwise regression, it was discovered that shareholder wealth was favorably correlated with dividend per share and lagged market price per share, but negatively correlated with retained earnings and the lagged price earnings ratio.

Bassam Jaara, (2018)- This study examines the factors that influence dividend policy for a sample of Jordanian non-financial enterprises between the years of 2005 and 2016. The historical dividend impact is almost always favorable and considerable, and it indicates the firm's trend of dividend payout rather than just paying out at random. Payout levels are negatively impacted by risk. The analysis was based on a number of hypotheses that have an impact on dividend policy, including the signaling theory, bird in hand theory, pecking order theory, and dividend irrelevance theory.

Werema (2018): A review of the firm's performance following adjustments to the dividend policy was done. Reversing a downward trend of poor performance, cutting dividends will also result in less financial leverage and liquidity issues. The results presented show that the market responds unfavorably to announcements of dividend reductions, which is consistent with findings from earlier studies.

(2008) David J. Denis In the US, Canada, UK, Germany, France, and Japan, larger, more profitable companies and those whose retained earnings account for a significant portion of total equity have a stronger inclination to pay dividends. There isn't much proof that the inclination to pay dividends and the relative valuations of companies that pay and don't pay them correlate positively outside of the US. Overall, our results challenge the legitimacy of the catering, signalling, and clientele explanations for dividends while bolstering agency cost-based lifecycle models.

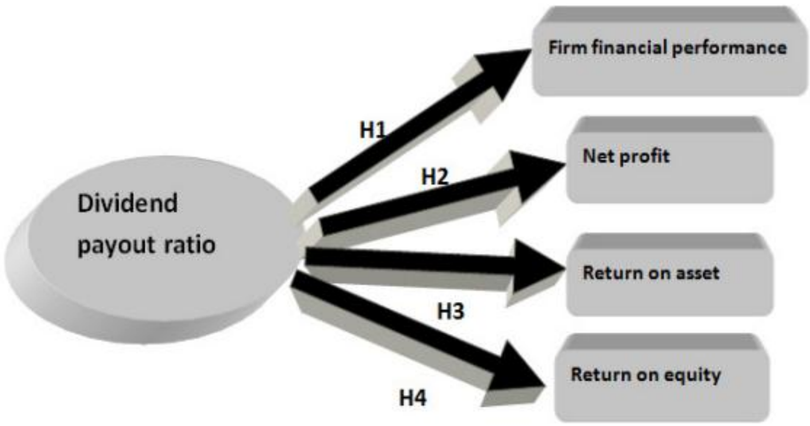
The authors of SAMY BEN NACEUR (2006) examine the dividend practices of 48 companies that were listed on the Tunisian Stock Exchange between 1996 and 2002. However, neither the concentration of ownership nor the use of financial leverage appears to have any effect on Tunisia's dividend policy. Additionally, the size and liquidity of the stock market have a negative impact on dividend payments. The outcomes are fairly adaptable to various specifications.

OBJECTIVES

1) To study various dividend policy ideas
2) To study and ascertain the connection between the dividend payout ratio and the financial success of the company.

RESEARCH METHODOLOGY

In this study, 20 Indian Pharma and textile firms with NSE listings that span five years (from 2016 to 2021) make up the sample. Information is gathered from the annual reports of the NSE-listed companies. To determine the relationship between the firm's financial performance and the dividend payout ratio, the financial information from the annual report—including dividend payments, ROE and ROA, net earnings, and total assets—is employed.



RESEARCH INSTRUMENT

To determine the relationship between the company's financial performance and dividend payout, the regression and correlational method is utilized. Regression analysis essentially reveals the strength and direction of the relationship between the dependent and independent variables. The variables' strength and direction are measured using a correlation analysis, which runs from +1 to -1. Regression and correlation analysis is a very straightforward statistical method for determining the relationship between dividend payout and firm financial performCorrelation & Regression Analysis

Correlation Analysis			
	Dividend Payout & NPAT	Dividend Payout and ROE	Dividend Payout and ROA
Correlation	0.698	0.712	0.236
Regression Analysis			

F Value	2.822	3.005	0.261
Dividend p Value	0.198	0.189	0.639
R Square	0.432	0.501	0.088
Coefficient	903.45	0.300	0.009

The findings show a significant positive link between dividend payout and ROE as well as a strong positive relationship between payout ratio and net profit after tax. Although there is a positive association between payment and ROA, it is a weak one (shown in Table). The findings of the regression analysis indicate that the R square value for NPAT and ROE is approximately 50%, however the 7.5% return on asset is rather low. The NPAT, ROE, and ROA intercept p values are 0.198, 0.189, and 0.639, respectively, demonstrating that dividend payout has a considerable impact on corporate financial performance. According to the coefficient value, increasing the dividend paid by one unit will result in a 0.009-unit rise in ROA and a 0.300-unit improvement in ROE. The awards and business financial performance have a strong positive association. The dividend payout ratio clearly has a major impact on the financial performance of the organization, as seen by the low p value and positive coefficient.

CONCLUSION

Finding the link between dividend payout ratio and firm financial performance of companies listed on the NSE was the main objective of this study. The association between payout ratio and corporate financial performance was ascertained using correlation and regression analysis. The following inference can be made in light of the findings and discussion already mentioned: As evidenced, dividend payout has a favorable effect on a company's financial performance (table). It displays how the dividend policy affects the company's financial results. The results show that the dividend payout ratio has a big effect on the company's financial performance. Due to this conclusion, the hypotheses H1, H2, H3, and H4 are accepted, proving that there is a positive correlation between dividend payout and FP, dividend payout and net profit after tax, dividend payout and ROA, and dividend payout and ROE. The results of the entire study show that the dividend payout affects the company's financial performance.

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