

# Impact of Dividend Policy on Firm Performance:

(Evidence from the Manufacturing firms in Pakistan)

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## Abstract:

*The basic resolution of this study is to investigate the relationship between dividend policy and firm performance. Design/methodology-the sample contain on 15 manufacturing companies in the year of 2014 to 2017.time series data were calculated from the financial statement of the selected manufacturing firms. Return on asset (ROA) and return on equity (ROE) were used as dependent variables while dividend payout ratio (DPOR), earning per share (EPS), price earnings ratio (PER) were modeled as independent variables. Multiple regressions like correlation, descriptive were used as data analysis techniques. Findings reveal that all the independent variable have a positive relationship with dependent variables. Dividend payout ratio, earning per share, price earnings ratio positively influence return on investment. Limitation of our study is that we examine only 15 manufacturing firms other researcher use large size sample and other sector firms expect manufacture.*

**Keyword:** Dividend policy, Performance, Dividend payout ratio, Price earnings ratio, Returns on the asset.

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## Introduction:

The purpose of this research is to investigate the impact of dividend policy on the firm's performance from manufacturing firms in Pakistan. dividend policy becomes the very important issue in the business field.in Pakistan firm, dividend policy creating many issues in the capital market.in recent decades many economists have analyzed the dividend policy. Black (1976) stated that "the harder we look at the dividend picture, the more it seems like a puzzle, with pieces that don't fit together". But the dividend policy also affects the firm profitability.

Dividend policy is the declaration of dividend payment to a shareholder. Dividend refers to the distribution of profit to their owners. The dividend also the benefit of a shareholder as a result of their risk.it is the decision of management to set the portion of profit that provides the shareholder according to their investment. Dividend policy is a small factor that describes the firm's performance.in finance dividend distribution decision is one most important area in four elements.

In Pakistan prudence and globalization well organized fast success in it provide know-how in firm intently. In the modern area firm demand to raise more innovation. Basically, it is essential for firms to formulate the dividend policy to improve the performance of a firm. Through dividend, the framework optimizes the power of the firm's progress . The dividend can exploit cut down the size of agency cost. The dividend may be classified in. (1) counsel (2) surplus. Administer trusted that dividend policy is a significant impact and directly affect the value of a share. The most advantageous policy decreased the overused of price and that provide guidance to decreased the shareholder's estate.

The domination of dividend effects the caliber of the firm and transformed into (blow of stream) sermonized functioning by Modigliani and Miller. That conferred the aspect of a firm's field of vision inappropriate its policy contrasted the bring home efficacy. The shareholders are hard-hearted in acquiring available sources like dividend or other gains an excellent market. Agency theory suggested by Jonson and Mackling (1976). The conductor perhaps inadequate to enlarge shareholder's abundance as long as no- accompaniment constitution of applicability affair and objective discrepancy. Jenson contends in case that comprehensive allotment of profit indemnified the dividend can improve the assessment of the firm as a result of authorizing deficient free of cost capital gains held by the managers. Dividend policy indicates association appointment as long as the dividend is famous beneficial for business adherence along with enduring circumstances scrutiny of firms.

We use different variables for measuring the impact of dividend policy on firm performance. DPOR, EPS, PER, use independent variables and ROA, ROE use as dependent variables. ROA, ROE, measure the firm performance. This research paper contains five parts: Ist is the introduction second literature review third methodology and fourth and fifth on result and analysis.

#### **The objective of the study:**

- The main purpose of this research is to find the impact of dividend policy may have on firm's performance of manufacturing firms listed in Pakistan stock exchange.
- To investigate the relation between ROA and dividend policy.
- To find the relationship between dividend policy and EPS.
- Is there any relation between dividend policy and firm's performance?
- Impact of dividend policy on investment.

#### **Research Question:**

- What is the relationship between dividend policy and firm performance?
- What is the relationship between dividend policy and ROA?
- (Amidu 2007)What is the relation between dividend policy and ROE?
- What is the relationship between dividend policy and earning per share?

#### **Literature Review:**

The performance of dividend policy is one greatest arguable issue in the corporate finance works and still retains its prominent place both in established and initial markets (Hafeez&Attiya, 2009) Originate that the succeeding features are significant effects in the volume of dividends waged, present and previous years' incomes, the year to year inconsistency of incomes, the growth of earnings and previous times' bonuses.

Febrile strait at all (2014) analyzed the effect of dividend payment on the profitability of firms by using the data of 90 firms during the period of (2003-2009). He used many regression methods. According to this research large size of dividend and consistency in dividend have a positive relationship with profitability. But the researcher has not any proof that dividend increase is a gauge of higher profit. Mohammed amid (2007) used data extracted from the financial statement of the listed firm on the GSC from recent 8 years. He used ordinary least squares model to analyze the regression equation. He finds out that ROA, dividend policy, and growth in sale positively associate with each other. But dividend payout ratio, ROA, and leverage have a negative relationship.

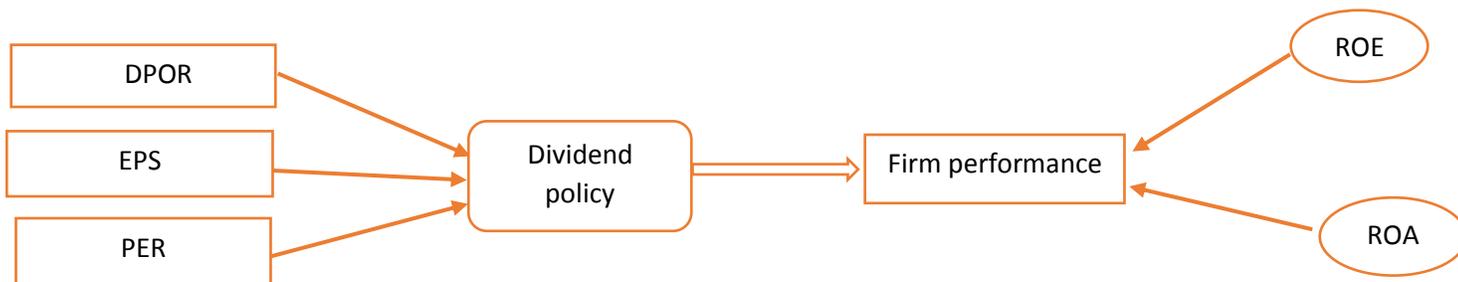
Mulanazar at all (2016) examined the dividend policy have any influence on the firm performance he collected the data from the financial statement of listed firms during the period of (2010- 2015). He used the OLS technique. Results show that ROA, dividend, and growth are negatively associated with each other. Dividend payout ratio and leverage negatively influence the ROA. T.Velnampy at all (2014) stated that there is any connection between dividend policy and firm's profitability by using data of manufacturing firms during the age of (2008-2012). He used ROA and ROE as an independent variable. EPS and dividend payout are determining the factor of dividend policy. He concludes that dividend payout and earning per share don't influence the firm performance.

Carless Yegon at all (2014) find out the relationship between dividend policy and firms profitability by taking 9 manufacturing firms listed in Kenya. Research tells that dividend policy to have a positive influence on firm performance. Dividend policy also positively effect on investment. Research recommends that the firm must have a strong dividend policy which will help them to earn profit and investment. (Khadija Farrukh at all 2017) purposed in this research about the dividend policy and impact of firm's profitability. Many firms used this policy because it had a direct relation with profitability. ROA is used to measure the performance of the firm this impact rely on different theories. Like bird in hand theory, signaling theory, and clientele theory.

(Priya, K at all 2013) determine how dividend policy influenced on firms performance through correlation and regression measure the impact of firms performance. The finding shows that the dividend policy based on return on investment, earning per share, and price earning. 51 firms paying a dividend from sequences 10 years to increase their wealth. Firms can reduce the agency cost through paying a dividend which creates attraction with employees. Jimoh JAFARU suggested through regression results the

interaction of dividend policy and profitability of the firm (2012). Due to a meaningful dividend payout policy can improve the economy of scale of firms and level of performance.

**Conceptual framework:**



**Research Methodology:**

This research examined the impact of dividend policy on firm performance. as a sample, we use 15 manufacturing firms listed in Pakistan stock exchange (PSE). Data collected from the company annual reports. The duration of this study is four years covering the period (2014, 2017). Our target population is Pakistan manufacturing firms (PSE). Our researcher used different methods for evaluating the data through descriptive, correlation and regression.

**Research Hypothesis:**

- H1:** There is any relation between dividend policy and firm performance.
- H2:** There is a positive relation between EPS and dividend policy.
- H3:** Return on asset has any relation to dividend policy and firm profitability.

**Mode of Analysis:**

The following dividend payout ratios and firm performance ratios are use

Dividend payout ratios	
Earnings Per Share	Net Income / Total Number of Capital
Price to Earnings Ratio	Market Price per Share / Earnings per Share
Dividend Payout Ratio	Total Dividends / Total Net Earnings x 100%
<b>Firm Performance Ratios :</b>	
Return on Asset	Return / Total Asset X 100
Return on Equity	Profit after interest & tax / Equity capital X 100

Table-1: Calculations of Dividend Policy Ratios and Firm Performance Ratios.

Multiple regression analysis was performed to investigate the impact of Dividend Policy Ratios on Firm Performance which the model used for the study is given below. Firm Performance = f (ROA; and ROE) It is important to note that the firm performance depends upon Earnings Per Share (EPS), Price to Earnings Ratio(P/E), Dividend Payout Ratio (DPOR), Since two Firm Performance Ratios Return on Asset (ROA) and Return On Equity (ROE). The following two models are formulated to measure the impact of Dividend Policy Ratios on firm

Performance is as follows.

$$ROA = \alpha_1 + \beta_1 EPS + \beta_2 P/E + \beta_3 DPOR + \epsilon \dots \dots \dots (1)$$

$$ROE = \alpha_1 + \beta_1 EPS + \beta_2 P/E + \beta_3 DPOR + \epsilon \dots \dots \dots (2)$$

Where  $\alpha$ , is constant,  $\beta_1$ ,  $\beta_2$ , &  $\beta_3$  are coefficients of variables,  $\epsilon$  is error term.

**Analysis and Interpretation:**

**Descriptive Analysis;**

Table 2: Descriptive Analysis

Variables	ROA	DPOR	EPS	PER
Mean	6.01343	43.28783	15.7753	13.3435
Maximum	26.7200	119.0200	53.4300	113.3435
Minimum	0.0200	0.0000	1.7100	1.5300
Std.Dev	7.8484	31.7317	12.9574	14.6129

The researcher used in mean, maximum, minimum and std. Dev checks the impact of dividend policy on firm performance. Descriptive analysis table 1 ROA mean 6.0134, dividend payout ratio 43.2878, earning per share 15.7753, and price earnings ratio 13.3435. The results of a standard deviation of ROA 7.84842, the dividend payout ratio 31.7317, earning per share 12.9574 and price earnings ratio 14.61297 of 15 manufacturing firms in Pakistan.

**Correlation Analysis:**

Table 3: Correlation Matrix for manufacturing companies

variables	ROA	DPOR	EPS	PER
ROA	1			
DPOR	0.6656	1		
EPS	0.3692	0.2261	1	-
PER	0.2952	0.1382	-0.0675	1

Correlation results find out the relationship between dividend policy on firm performance in Pakistan. The results ROA significant correlate with Dividend payout ratio, earning per share and price earnings ratio.

**Regression Results:**

Regression analysis Table 4:

Variable	Coefficient	Std.Error	t-statistic	Prob.
DPOR	0.111658	0.021779	5.126963	0.0000
EPS	0.076381	0.052316	1.460000	0.1498
PER	0.069291	0.047838	1.448456	0.1530

Regression model used in researcher analysis the R- Squared 0.479417 are significant results overall models show that variables are significant. The probability of DPOR is 100% significant and EPS probability of 0.14% is acceptable. Because of 5%, 10% and 15% chances of error in secondary data. Price-earnings ratio has 0.15% error of chances.

**Limitations:**

Firstly the sample size of our research is too small. We use only 15 manufacturing firms.

Secondly, we use only 4-year data (2014 to 2017).future researcher can use more year data for the better result. We use only manufacture sector other researcher use different sector for their research We use only ROA, ROE, DPOR, EPS, PER but the upcoming researcher can use different variables for their greatest and, more valid result. Finally, they use multiple methods in spite of the regression method.

**Conclusion:**

The main objective of this study is to inspect the impact of dividend policy on firm's performance listed in Pakistan stock exchange (PSE). for the research purpose, we select 15 manufacturing firms in Pakistan. Data were obtained from the annual reports during the period of 2014 to 2017.we evaluated the data through correlation, descriptive and regression analysis. Table 4 shows that there is a positive relationship between return on asset, dividend payout, earning per share and price earnings ratio. The result of Table 4 shows that the dividend payout ratio has a positive effect on return on asset.in the last we recommend that firms should maintain consistency In dividend policy to increase in return on asset.

**Future Direction:**

The main focus of this paper is only on the 15 manufacturing firms of Pakistan. For the future research can be added to the other sector and increase the sample size for the more accurate result. The result of this paper based on limited data for a limited time period so, increase the time period for future research. So, the further research can be conduct by taking the other companies, increase data and increase the time period.

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