Review Article

DIVIDEND POLICY AND FINANCIAL PEROFRMANCE- A STUDY OF QUOTED MANUFACTURING FIRMS IN NIGERIA AND KENYA

ABSTRACT

Several studies have been carried out on the effects of dividend policy on financial performance. This study was conducted to compare the position of this discuss between Nigeria and Kenya. The study proxied dividend policy by the dividend per share (DPS) of the sampled companies in Nigeria and Kenya while the Returns on Asset (ROA) was adopted to represent the financial performance of the sampled companies. The study thus found out that there is a significant positive effect of dividend policy on the financial performance in Nigeria and Kenya as revealed by the t-statistics of the result. The study therefore recommended that companies should pay close attention to their dividend policies because it has a significant effect on the financial performance of companies.

Key Words: Dividend Policy; Dividend per share; Return on Asset; Total Asset

1.0 INTRODUCTION

There are three major functions of investment goals that the modern business entities are engaged to fulfil; the investment decision, the financing, and the rewarding policy. The challenge of financial managers has been on dividend policy entailing the pay-out ratio and the retained earnings for growth (Pandey, 2010). One of the foremost studies carried out on dividend policy was that of signalling by Litner (1956) and was the first to identify the information that the managers assess current earnings to determine the level of dividend to be paid. Mayo (2008) stated that retained earnings is the most significant source of long term financing and dividends should be paid in the absence of projects with positive net present value. Booth and Cleary (2010) explained that and exclusive decision by management to pay dividend with what percentage of retained earnings and what portion is referred to as dividend policy. Nwude (2003) defined the dividend policy term as the managerial principle for sharing company's net profit after taxes between residual shareholders and retained earnings in a given financial year. Emekekwue (2005) explained dividend policy as the portion of firm earnings that will be held back as retained earnings. Huda and Farah (2011) observed dividend policy is an issue of interest in financial works.

Financial performance review helps examine the business goals and plan effectively for improvement. It also measures how well the money invested is performing viz-a-viz alternative investment forgone (NIB 2019). According to NIB, margins (gross, net profit, operating expenses) and returns (assets and capital employed) are good performance indicators. Particularly, manufacturing companies may be assessed by working capital, cost base, operating expense margin, return on asset. Abolo (2005) points out that a successful manufacturing sector is of significant to every modern economy. This is because manufacturing sector drives real development and growth and the main challenge of this sector is cost. By 2030, operational expenditure in manufacturing in Africa is projected to reach $666.3 billion, with $201.28 billion more than it was in 2015, (Signé 2018).

In Nigeria, manufacturing sector operates under unfavourable environment, records show that over 270 firms closed down in 2016 due to no patronage of their products in Nigeria and abroad and many laid off workers and others cut down production. Expectedly, the contribution to the GDP is 4.19% averagely (Abolo, 2017). In Kenyan economy, manufacturing firms have not fully realized hteir potential due to poor market access, restrictive legislation, high cost of credit, poor infrastructure and inadequate capacity to meet product quality standards (Kenya Engineer 2014). The contribution of the sector to gross domestic product (GDP) has stagnated at 10% and 8.4% in 2017. With concern, The Big 4 Agenda in Kenya predicts increase in GDP to 15% by 2022. In these two economies, the financial performance is affected by low capital injection. Foreign and local investments in industries and infrastructure are low, this may be due to poor business environment or politics.

This study seeks to make its contribution to the dividend policy empirical literature in several important ways. One, to examine a different approach to evaluating the effect of Dividend policy on financial performance proxied by Return on Asset (ROA), focusing on two developing countries; Nigeria and Kenya. Again, dividend policy can be associated with size of companies in developing dividend policy that can significantly affect financial performance. This factor is not directly related to financial performance. The study considers the role of company size in explaining the relationship between dividend policy and financial performance as a moderating variable.

Previously, several studies have been on dividend policy and its effect on wealth maximisation, share price performance and market price of share, most works also evaluate financial sector. Despite the benefits of the findings, manufacturing sector in developing economies like Nigeria and Kenya is considered. Hence, the evaluation of their financial performance based on the quality of dividend policy adopted.

2.0 LITERATURE REVIEW

2.1 Conceptual Review

Basically, dividend policy deals with rules involving the payment of cash dividend now or an increased dividend in the future. These are largely determined by the companies retained earnings and the capacity to generate constant returns on investments. A company's dividend policy must optimize capital gains, Pandey (1999). Share repurchases, share split, cash and share issues are forms of dividend which are paid out of retained earnings or current year earnings. Investors placed importance on dividend constancy. It was observed that investors prefer to measure firms'

performance through dividend payment instead of declared earnings and this is as a result of inaccurate information about the corporation performance. Naceur, Samy, and Goaied, (2002).

The dividend is a form adjustments given on the profits made and it is shared after the approval of shareholders, once a year. This explains the reason investors, invest in stock market to obtain the gains on investment, Idawati, W. and Wahyudi, A. (2015).

In evaluating the productivity of the company, earnings generated can be compared with total assets (ROA). High interest due to the confidence of investors to performance management that is able to manage the resources of its assets into profits. The greater the profit generated, the level of stock return expected by investors will be greater or a positive value. More so, investors will be inclined to invest in shares in these companies. This will lead to an increase in demand for stocks in the stock market. Assuming that the number of shares outstanding remains, it is certain that the stock price will move higher. Arifin (2002) states that "The higher the ROA the higher the company's ability to generate profits, the higher the company's income would make investors interested in the stock value". This is in line with the opinions expressed by Pasaribu, (2008) that the "fundamental factors that are often used to predict the stock price or stock returns are financial ratios and market ratios. Financial ratios serve to predict stock prices, among others, return on assets (ROA)''.

Arthur J. Keown, (2008) stated that the return on assets ROA can be used as a pointer of the cost-effectiveness of the company. Return on assets regulate the amount of revenue generated from the assets of the company by linking the net revenue to total assets. ROA can describe how effective the company utilizes its assets into profit. Investopedia suggests that: The ROA gives investors an idea of how efficiently the firm is translating the money it has to capitalize into net revenue. The higher the ROA number, the better.

2.2 Empirical Review

Chelimo, J. K. and Kiprop, S. K. (2017) establish the effect of dividend policy on share price performance of listed insurance firms at NSE Kenya; using dynamic regression analysis and from the findings conclude that, dividend policy decisions affect share price. This is because it makes prices of stocks move either up or down depending on dividends policy by management.

As revealed by Malakar and Gupta (2002), dividend policy has significant influence on earnings per share. Tuli, Nishi and Mittal (2001) in their cross-sectional analysis of earnings ratio of 105 companies found financial performance, driven by sound dividend policy to be significant in share price determination.

Malhotra (1987) studied four industries and found that earnings per share (financial performance) had positive and significant influence on market price of equity share. Kumar and Hundal (1986) used the linear regression model and examined the impact of dividend policy on market price of share. BalKrishnan (1984) applied correlation and multiple linear regression techniques on 22 firms out of five variables, financial performance remained significant determinant of market price.

Also, the suggestion of Glen, Karmokolias, Miller, and Shah (1995) is that Dividend Policy in emerging economies is different to those in developed economies. Looking also at firms' performance, (Kopcke, 1992) finding was that insurance firms are probably going to produce possible

indicator through policy decisions on dividend if their market value is more undefined due to intrinsic peril of irregular information amid the stockholders and upper management.

Ogolo (2012) did a study on impacts of dividend policy on share price performance concentrating on companies listed in Kenya Stock Exchange market of Nairobi for time series of 2003 to 2012. 38 local and multinationals firms were sampled for analysis, using panel data. The findings were that a significant relationship exists between market price performance, measuring three independent variables namely; dividend per share, earnings per share and dividend payout ratio.

2.3 Theoretical Review

Many theories on dividend payment have been applied on this research and they are based on the understanding, the development and decision to reward the shareholders. This study adopts the bird-in-hand theory, which was developed by Gordon and Walter (1963) which concluded that investors always prefer cash in hand rather than a future promise of capital gain.

Also, the catering theory by Baker and Wurgler (2004) suggests that managers pay dividend according to the needs and wants of the shareholders, this measures the efficiency of financial managers' balancing of investment and rewarding functions.

Under the signaling Hypothesis Theory, though Modigliani and Miller (1961), assumed that there is perfect knowledge about a firm by investors and management, studies counter that as management looks after the firm, there is timely and concise information about the firm than outside investors know and impliedly, information knowledge should enhance performance.

Lintner (1956) suggested that dividend payment pattern of a firm is influenced by the current year earnings and previous year dividends. As such, dividend may be viewed as the free cash flows comprising of cash balance after all positive investments have been considered (Damodaran, 2002).

The decision as stated by Pandey (2005), is an important one for the firm as it influences financial structure and stock price of the firm. The dividend payment ratio is a major aspect of the dividend policy of the firm, which affects the value of the firm to the shareholders (Litzenberger and Ramaswany,1982).

3. METHODOLOGY

3.1. Research Design

Expost facto research design was adopted in this study. Secondary data were obtained from the annual reports and accounts of ten (10) companies (five per country) for a period of 10 years (2008-2017). In order to generate reliable and factual findings; this research adopted the combination of descriptive, historical and regression analysis. A descriptive analysis; according to Kothari (2004) is the arrangement of conditions for collection, analyzing and interpretation of data in a way that brings out the importance of a research purpose, with economic perspective in a procedural way. So also, Chandran (2004) defines historical design as a way to gather, verify and validate evidence obtained from past financial information to establish facts, and the secondary data must be reliable, relevant and sufficient.

3.2 POPULATION AND SAMPLING TECHNIQUES

The population of this study consists of all listed companies in Nigeria and Kenya's stock exchange markets. Convenient sampling method was utilized to select five (5) companies from each of countries for the purpose of this study.

3.3 MODEL SPECIFICATIONS

Two models were adopted for this study. This was because two measurements of financial performance (ROA and EPS) were considered. The following are the models adopted for this study;

$ROA_{it} = \beta_0 + \beta_1 DPS_{it} + \beta_2 SIZE_{it} + \varepsilon$

Where;

ROA = Returns on Assets

DPS = Dividend per share

SIZE = Size of each company measured by the natural logarithm of Total Asset

ε = error term

5.0 FINDINGS AND DISCUSSION

5.1 Descriptive Analysis

Table 1 shows the summary statistics of all the variables. The mean values of ROA, EPS, SIZE and DPS were 0.165, 79.080, 17.97, 160.33 for Nigeria and 0.72, 65.78, 16.18, and 0.87 for Kenya respectively. This figures when compared to the values of the standard deviation which measures the dispersion or spread in the data set from its mean, showed the extent of volatility of the variables data set. For instance, the Nigeria's EPS standard deviation is 282.09 while its mean is 79.08, and for Kenya, standard deviation is 285.56 while the mean was 65.78, this gap suggests the presence of a higher volatility in the EPS of both countries. This can also be seen in the difference between the minimum and maximum values for both countries i.e. -16 and 15565 for Nigeria and -5.83 and 1938 for Kenya.

The negative minimum values of ROA for both countries suggest that some of the sampled companies made losses during the period sampled for this study. Likewise, the minimum values of DPS for both countries indicated that there are some out of the sampled companies for the sampled periods did not pay dividends to their shareholders.

Table 1: Descriptive Statistics

	NIGERIA				KENYA			
	Mean	Std. Dev.	Minimum	Maximum	Mean	Std. Dev.	Minimum	Maximum
ROA	.1645271	.2980386	-.1276591	1.840513	.0720989	.0982204	-.2142759	.3127907
EPS	79.08012	282.0915	-16	1565	65.78328	285.5564	-5.83	1938
SIZE	17.97372	.919092	15.17941	20.47131	16.1838	285.5564	13.39547	18.90153
DPS	160.3348	486.1621	-5.135615	2559.999	.8730977	1.393904	-.015	5

Source: Researcher's study 2019

5.2 Empirical Analysis

5.2.1. Diagnostic Tests

Relevant diagnostic tests were performed on the data set to validate their suitability for the model estimations. The hausman test was carried out to determine whether fixed or random effect is suitable for the models. The result of the test however, indicated that the models do not meet the assumptions of the hausman specification test hence the adoption of the pooled ordinary least square (OLS) for both models. The study went further to perform the heteroscedasticity and serial correlation tests. These tests were performed to determine the presence or otherwise of heteroscedasticity and autocorrelation in the models. The test results therefore informed the use of the option that produced robust standard errors through the use of STATA. The regression results are therefore presented in Table 2

Table 2: Regression Result

	NIGERIA				KENYA			
Variable	**Coefficient**	**Std Error**	**t-Stat.**	**Prob.**	**Coefficient**	**Std Error**	**t-Stat.**	**Prob.**
Constant	2.759949	1.509404	1.83	0.074	-.3741439	.123692	-3.02	0.004
DPS	.0001465	.0000852	1.72	0.092	.0282999	.0077396	3.66	0.001
SIZE	-.1457079	.0828131	-1.76	0.085	.0260467	.0074955	3.47	0.001
F-Statistic	2.23				9.96			
Prob.(F-Stat)	0.1185				0.0002			
Adjusted R-squared	0.2565				0.2525			
Diagnostic Tests								
Heteroskedasticity test	62.32			0.0000	0.22			0.6416
Wooldridge test for autocorrelation	3.842			0.1215	0.093			0.7756

Dependent Variable: ROA

Source: Researcher's study 2019

5.2.2 Interpretation of Result (Model One)

The regression estimate revealed that there is a positive relationship between DPS and ROA for both countries. This is indicated by the sign of the coefficients β_1 = 0.0001465 and 0.0283 for Nigeria and Kenya respectively. However, with respect to Size, there exist a negative relationship between ROA and the Sizes for Nigeria and a positive relationship for Kenya. This is also depicted from the sign of the coefficients β_2 = -0.1457 and 0.0260 for Nigeria and Kenya respectively. The t-statistics for the DPS and Size shows that these individual relationships were all significant at 10% i.e. lower than 10% level of significance however, the f-statistics indicated that the entire model for Nigeria was not significant but the model for Kenya was significant. This was depicted by the probabilities of the t-statistics of 0.092 and 0.085 for Nigeria's DPS and Size respectively and 0.001 and 0.001 for Kenya's DPS and Size respectively. Likewise, the probability of f-statistics of 0.12 and 0.0002 for Nigeria and Kenya respectively.

The adjusted R-squared for the model shows the extent of changes in ROA caused by the joint influence of IFRS adoption and Size of the sampled companies. The result depicts that 26% percent of changes in the ROA of Nigeria is caused the variables in this model while 25% of the ROA of Kenya is caused by the two variables. The other 74% of changes in Nigeria's ROA and 75% changes in Kenya's ROA must be caused by other variables not included in this model.

Thus, from the result in Table 2, the null hypothesis that dividend policy has no significant effect of financial performance of listed firms is hereby accepted for Nigeria and not accepted for Kenya.

6. CONCLUSION

This study focused on the effect of dividend policy on the financial performance of listed firms in Nigeria and Kenya. This was achieved by representing the dividend policy by the dividend per share of the selected firms. The financial performance was represented by Returns on Asset (ROA) and size was also introduced to control the effect between the dividend policy and financial performance. The study found out that there is a significant effect of the dividend policy and size jointly on financial performance of Kenya while the result for Nigeria showed that there was no significant influence on dividend policy and Size jointly on the financial performance of the sampled firms. This may be attributed to the different culture or regulations of firms in the Nigeria and Kenya. It was therefore recommended that firms in Nigeria and Kenya should pay close attention to their dividend policy has it significantly affects the financial performance of firms.

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