



Dividend Policy and Financial Performance- A Study of Quoted Manufacturing Firms in Nigeria and Kenya

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Authors' contributions

This work was carried out in collaboration among all authors. Author MBA designed the study, performed the statistical analysis, wrote the protocol and wrote the first draft of the manuscript. Author ATA managed the analyses of the study. Author OTO managed the literature searches. All authors read and approved the final manuscript.

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ABSTRACT

One of the indicators of shareholders' wealth maximization is dividend policy (DP) consistency, proxied by dividend per share (DPS) with moderating variable of company size and financial performance measured by the return on asset (ROA). The purpose of this study is to demonstrate the significance level of changes in ROA based on DPS comparing manufacturing companies in Nigeria and Kenya. The data used in this study is the use of panel data method and Convenience Sampling is applied and data analyzed by comparing the regression model, Ordinary Least Square (common effect). The results indicate that there is a significant positive effect on ROA in Kenya manufacturing companies, while Nigeria's records insignificant negative effect as revealed by the t-statistics due to DP. These undeveloped economies' relevant sector for growth is the manufacturing and is the focus of this study. The paper concludes by recommending that Kenya and Nigeria manufacturing companies should focus on DP.

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1. 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 [1]. One of the foremost studies carried out on dividend policy was that of signalling by [2] and was the first to identify the information that the managers assess current earnings to determine the level of dividend to be paid. Mayo [3] 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; [4] explained that an exclusive decision by management to pay dividend with what percentage of retained earnings and what portion is referred to as dividend policy. Nwude; [5] 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. Emekekekwe [6] explained dividend policy as the portion of firm earnings that will be held back as retained earnings. Huda and Farah; [7] 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 [8] 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, [9] 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, [10].

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. Many companies laid-off their workers and others cut down production. Expectedly, the contribution of the sector to GDP is 4.19% on an average [9]. In Kenyan economy, manufacturing firms have not fully realized their potential due to poor market access, restrictive legislation, high cost of credit, poor infrastructure and inadequate capacity to meet product quality standards [11]. 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. 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, [12]. 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 [13].

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, [14].

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; [15] 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 [16] 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)".

Keown [17] 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

Joseph and Symon; [18] 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 [19], dividend policy has significant influence on earnings per share. Tuli and Mittal [20] 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; [21] 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 [22] used the linear regression model and examined the impact of dividend policy on market price of share. Balkrishan [23] 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 et al.; [24] is that Dividend Policy in emerging economies is different to those in developed economies. Looking also at firms' performance, [25] 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 [26] 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.

Economically; in Kenya, out of US\$1.7 trillion global value of the fashion sector & many

countries exporting; Bangladesh did US\$33 billion Apparel Exports in 2017 with 5 million direct jobs in the sector against Kenya US\$360M & 52000 direct jobs, therefore, job opportunities abound, Meanwhile, the illicit trade is a major menace to the textiles and apparels market. The un-customed products for textiles and apparels market is approximated to be Ksh. 48 Billion. This is about 2 times the value of local textiles and apparels manufacturing turnover. As such, the government is losing about Ksh. 21.36 billion from 16% VAT, 25% CET, 1.5 RDL and 2% IDF charges [27].

In Nigeria, major challenge is power generation capacity which is less than 4000 Megawatt, about 20 per cent of the estimated national demand. Also, infrastructural Deficit is recorded by the figures released recently by the National Electricity Regulatory Commission (NERC) which indicates that of the N796 billions spent to fuel generators in 2008, members of Manufacturers Association of Nigeria (MAN) spent over N350 billion. Another challenge is that of manufacturing sector operating below capacity at 47% in 2009 and 45% in 2010, losing business opportunities, incurring losses and closing shops. MAN, officially declared that of its 2000 members, 30 percent mostly small and medium scale industries (SMEs) have closed down, 60 percent of them ailing while just 10 percent of them, notably the multinationals currently operate at sustainable level [9].

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; [28] 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 ;[29] 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 [30], 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; [2] 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 [31].

The decision as stated by Pandey; [1], 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 [32].

3. METHODOLOGY

3.1 Research Design

Expos 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 ;[33] 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, [34] 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. Convenience sampling method [35] 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

4. FINDINGS AND DISCUSSION

4.1 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.

4.2 Empirical Analysis

4.2.1 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.

4.2.2 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 $\beta_1 = 0.0001465$ 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 $\beta_2 = -0.1457$ 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.

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

Table 2. Regression result

Variable	Nigeria				Kenya			
	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. CONCLUSION

This study focuses on the effect of dividend policy on the financial performance of listed firms in Nigeria and Kenya. Empirical studies focus on banks, insurance companies, oil and mining and effects of DP on EPS, ROA and Stock Price. 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 of dividend policy. This may be attributed to the different culture or regulations of firms in Nigeria and Kenya. This study, therefore recommends that manufacturing companies pay close attention to dividend policies. Generally, changes in DPS will affect ROA and companies in Nigeria need to improve on DP while Kenya set needs concentration on moderating variable 'Size'. The limitation of this work is the inconsistencies in matching companies' annual reporting periods and dividend declarations. This is largely owed to non-standardized financial reports in Kenya and local companies evaluated. In addition, mostly multinationals were selected in Nigeria and dividends were not paid in periods that losses were reported. The study may limit the application of the findings, however, future or similar research to be undertaken may select listed manufacturing companies of similar size and status.

COMPETING INTERESTS

Authors have declared that no competing interests exist.

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