Determinants of Dividend Policy in India – Special Reference to Nifty 50 Companies

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Abstract

Dividend policy is the firm's policy considered to structure the dividend payout of the shareholder of the company. Various factors are responsible for determining the dividend payout of the firm. In this research paper, we are exploring the determinants of the dividend policy of NSE, Nifty 50. This paper studies the impact of six basic variables on the dividend payout of NSE, Nifty 50 Index companies for the financial year 2015-16 to 2019-2020. These factors include liquidity, leverage, firm size, return on equity, risk and tax rate. Multiple regression analysis was used to study the impact of selected variables on the dividend policy of the companies under study. The results reveal that return on equity has a significant positive impact on dividend payout, whereas risk and tax rate have a significant negative impact.

In contrast, there is a positive relationship and zero significance was found between liquidity and dividend payout and leverage and dividend payout. A negative relationship and no significance was found between the size of the firm and dividend payout. This means that liquidity, leverage and size of the firm failed to have any significant impact on the dividend payout of the companies under study.

Keywords: Dividend payout, Liquidity, Leverage, Risk, Size of the firm, Tax rate.

Introduction

The dividend is a distribution of profits by a company to its shareholders. When a company earns profits, it can either distribute it as a dividend to its shareholders, or the company can retain the profits or invest it back into the business, i.e. retain earnings. Dividend policy is one of the most important decisions concerning the distribution of profit to the shareholders of the company. The ultimate objective of a finance manager is the maximisation of shareholder's wealth. Dividend policy is different from sector to sector and company to company.

There are a lot of factors that affect the dividend decision of the firm. This emphasis of the study is on exploring the factors which determine the dividend policy of the companies listed on Nifty 50.

Review of Literature

Aryan Majumdar (2017), in his study, observed that profitability and past dividend are positively affecting the dividend payout ratio and liquidity; free cash flow and growth are negatively affecting the dividend payout ratio. In contrast to this, leverage, firm size and life cycle failed to impact the dividend payment during the study period.

Anjana and Balasubramanian (2017) observed that the financial performance of firms has a significant positive impact on dividend policy decisions. A firm with high profits has the potential to pay dividends more than less profitable firms. Firm size is positive and significant. Larger firms have easier access to funding and can distribute dividends to shareholders better than smaller firms.

Srinivasa and Hari Krishna (2018), in their study, found that there is a significant association between the dividend amount and return on equity, debt-equity ratio and institutional holdings. There is no significant association between dividend amount and tax rate and type of industry it belongs to at a 1% level of significance.

Venkataramanaiah, Madhavi and K. Shiva (2018), in their study, established a positive and significant relationship between Return on Equity (ROE), i.e. organisation's economic performance and dividend pay-out policy, while it was also concluded that there is a significant negative relationship between size and dividend policy and a negative relationship and no significance in between liquidity, leverage and dividend pay-out policy of the listed sample companies of Nifty 50.

Sangeetha (2018), in her study, observed that factors like liquidity, profitability, Inflation and size of the firm have a significant negative impact on dividend policy on the NSE firms considered for the study, while the risk variable has a negative and significant impact. According to the study investment opportunities, the lagged dividend, yield curve and taxation do not play a significant role in determining the dividend policy.

Zakir (2016) concluded that last year's dividends, firm growth and liquidity positively affected the dividend payout ratio. Some other factors like profitability and leverage negatively impact the dividend payout ratio. There are few factors such as Risk, Ownership and size of the firm which do not have a direct impact on the dividend payments. Thus, key determinants of dividend payout in the study include leverage, liquidity, firm growth, previous year's dividends, and profitability.

Thirumagal and Vasantha (2017), in their study, identified the determinants of dividend payout in selected five industries viz., Infrastructure & construction, energy, information technology and pharmaceutical industry and found that leverage, past dividend, size of the company, firm risk and profitability were the major determinants of dividend.

Souvik Banerjee (2016) analysed 4 Information Technology (IT) companies in India over 5 financial years to find the determinants of dividend policy. He found three factors, namely Leverage, PE Ratio, and Return on Equity, to be statistically significant, as far as Dividend Distribution Decisions are concerned.

Research Methodology

A diagnostic research design is used in the current study. The population for the data collection is the companies listed on National Stock Exchange (NSE). The sample size is 50 companies listed on Nifty 50, NSE. (i.e. N= 50). The study is built on secondary data. The required data is extracted from the concerned company's financial statements in the annual reports and websites for the past 5 years, i.e. from 2015-16 to 2019-20. Multiple-regression analysis along with correlation analysis is used as the statistical tool in the study. Multiple regression analysis is used to verify the hypotheses.

Variables Under Study

In this study, the Dividend Payout Ratio of the firm is taken as the dependent variable, whereas liquidity, leverage, size of the firm, ROE, risk(PE) and tax rate are taken as the independent variables.

Dividend Payout (DPR)

To analyse the dividend policy of the selected companies, the dividend payout ratio (DPR) has been used as the indicator of the dividend policy adopted by the companies under study. The dividend payout ratio is calculated as the total amount of dividend paid by the Net Income of the firm.

Liquidity (CR)

It is measured as the current ratio, which is computed as current assets divided by current liabilities. In this study, liquidity is expected to have a positive relationship with DPR. It is anticipated that a firm with higher liquidity tends to pay higher dividends due to excess cash and vice versa.

Leverage (DER)

The debt Equity ratio is a capital gearing ratio calculated considering debt (Long Term Debt of Firm) and Shareholders Equity. It is expected to have a negative relationship with DPR because a company having more leverage and frequent interest payments will have to decide on a low dividend payout because interest payments affect the cash position of the company, on cash flows during the year and on profits available for distribution of dividends and vice versa.

Size of the Firm

In this study, it is measured using LOG (Total assets). It is expected to have a positive relationship with DPR because it is anticipated that the larger the firm's size, the more is the tendency of the firm to pay dividends.

Return on Equity (ROE)

It is measured as the ratio of net income to equity shareholder's fund. If the profits of the company are higher, it is likely to pay a higher dividend as it indicates good financial health. Hence, a positive relationship with DPR is expected.

Risk (PE)

It is measured as PE ratio, the price of a share divided by the earnings per share. The P/E ratio is considered as a proxy for risk.

In the case of a higher P/E ratio, it is easy to predict future earnings/expected returns, which helps the investor minimise the risk factor and the dividend paid will be more. Similarly, in the case of a lower P/E ratio, it is more challenging to forecast the future earnings and return, which would decline the payout ratio. Hence, a negative relationship with DPR is expected.

Tax Rate

It is measured as the ratio of corporate tax to Earnings Before Tax (EBT). The corporate taxes directly decrease the residual earnings after-tax available for the shareholders. Therefore, a negative relationship of tax rate with DPR is expected.

Objective

To explore the factors which determine the dividend policy of the companies listed on NSE, Nifty 50.

Hypothesis

H_0^1: There is no significant impact of leverage on dividend pay-out.

H_0^2: There is no significant impact of liquidity on dividend pay-out.

H_0^3: There is no significant impact of risk on dividend pay-out.

H_0^4: There is no significant impact of return on equity on dividend pay-out.

H_0^5: There is no significant impact of the tax rate on dividend pay-out.

H_0^6: There is no significant impact of the Size of the firm on dividend pay-out.

Data analysis

Table 1: Results of Correlation and Multiple Regression Analysis

Variable	Correlation	P Value	Conclusion
Leverage	-0.33092	0.20343373	Insignificant
Liquidity	0.07405	0.38700909	Insignificant
Risk	-0.26492	0.048544868	Significant
Return on Equity	0.515323	0.004048705	Significant
Tax Rate	-0.23883	0.00474501	Significant
Size of the firm	-0.3923	0.613606788	Insignificant

Interpretation

Leverage

The results of multiple regression analysis showed the p-vale is 0.20343373>0.05. Therefore, it can be said that it is insignificant. The result of correlation shows a negative relationship between leverage and dividend payout, which is in line with our expectations. This means that leverage has a negative relationship but no significant impact on the dividend payout. Hence, H0b is accepted.

Liquidity

The results of multiple regression analysis showed the p-vale is 0.38700909>0.05. Therefore, it can be said that it is insignificant. The result of correlation shows a positive relationship between liquidity and dividend payout, which is in line with our expectations. This means that liquidity has a positive relationship but no significant impact on the dividend payout. Hence, H0a is accepted.

Risk

The results of multiple regression analysis showed the p-vale is 0.048544868<0.05. Therefore, it can be said that it is significant. The result of correlation shows a negative relationship between risk (PE) and dividend payout, which is in line with our expectations. This means that risk has a significant negative impact on the dividend payout. Hence, H0e is rejected.

This means the more the P/E ratio, the lower the risk and the more is the dividend payout and vice versa.

Return on Equity

The results of multiple regression analysis showed the p-vale is 0.004048705<0.05. Therefore, it can be said that it is significant. The result of correlation shows a positive relationship between ROE and dividend payout, which is in line with our expectations. This means that ROE has a significant positive impact on the dividend payout. Hence, H0d is rejected.

This means that the higher the firm's profits, the more likely it is that the firm will pay a higher dividend.

Tax Rate

The results of multiple regression analysis showed the p-vale is 0.00474501<0.05. Therefore, it can be said that it is significant. The result of correlation shows a negative relationship between tax rate and dividend payout, which is in line with our expectations. This means that the tax rate has a significant negative impact on the dividend payout. Hence, H0f is rejected.

This means if the corporate taxes are more, the residual earnings after tax of the company which is available for the distribution of dividends will decrease; hence lower dividends will be paid and vice versa.

Size of the Firm

The results of multiple regression analysis showed the p-vale is 0.613606788>0.05. Therefore, it can be said that it is insignificant. The result of the correlation shows a negative relationship between the size of the firm and dividend payout, which is not in line with our expectations. This means that the firm's size has a negative relationship but no significant impact on the dividend payout. Hence, H0c is accepted.

Findings and Conclusion

The paper studies the impact of liquidity, leverage, firm size, return on equity, risk and tax rate on the dividend payout of the companies listed on NSE, Nifty 50 for the financial year 2015-16 to 2019-20. It is found that the dividend amount of the companies under study has an association with various factors. Some factors are positively associated, while some are negatively associated with the dividend payout. Based on the above analysis, it can be concluded that the return on equity has an insignificant positive impact. In contrast, risk and tax rates have a significant negative impact on dividend payout. In contrast, there was a positive relationship found between liquidity and dividend payout. In contrast, no significance was found between leverage and dividend payout, and a negative relationship and no significance was found between the size of the firm and dividend payout.

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Appendix

List of NSE, NIFTY 50 listed companies for the study

S. No.	Name of NSE, Nifty 50 Listed Firm	S. No.	Name of NSE, Nifty 50 Listed Firm
1	Adani Ports & Special Economic Zone Ltd.	26	Infosys Ltd.
2	Asian Paints Ltd.	27	Indian Oil Corporation Ltd.
3	Axis Bank Ltd.	28	ITC Ltd.
4	Bajaj Auto Ltd.	29	JSW Steel Ltd.
5	Bajaj Finance Ltd.	30	Kotak Mahindra Bank Ltd.
6	Bajaj Finserv Ltd.	31	Larsen & Toubro Ltd.
7	Bharti Airtel Ltd.	32	Mahindra and Mahindra Ltd.
8	Bharat Petroleum Corporation Ltd.	33	Maruti Suzuki India Ltd.
9	Britannia Industries Ltd.	34	Nestle India Ltd.
10	Cipla Ltd.	35	NTPC Ltd.
11	Coal India Ltd.	36	Oil and Natural Gas Corporation Ltd.
12	Divis Laboratories Ltd.	37	Power Grid Corporation of India Ltd.
13	Dr. Reddy's Laboratories Ltd	38	Reliance Industries Ltd.
14	Eicher Motors Ltd.	39	State Bank of India
15	GAIL India Ltd.	40	SBI Life Insurance Company Ltd.
16	Grasim Industries Ltd.	41	Shree Cements Ltd.
17	HCL Technologies Ltd.	42	Sun Pharmaceutical Industries Ltd.
18	Housing Development Finance Corporation Ltd.	43	Tata Motors Ltd.
19	HDFC Bank Ltd.	44	Tata Steel Ltd.
20	HDFC Life Insurance Company Ltd.	45	Tata Consultancy Services Ltd.
21	Hero MotoCorp Ltd.	46	Tech Mahindra Ltd.
22	Hindalco Industries Ltd.	47	Titan Company Ltd.
23	Hindustan Unilever Ltd.	48	UltraTech Cement Ltd.
24	ICICI Bank Ltd.	49	UPL Ltd.
25	Induslnd Bank Ltd.	50	Wipro Ltd.

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