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"A Study on Dividend Policy and Its Impact on behaviour of Listed Manufacturing Companies in India"

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ABSTRACT

The present study examines the dividend behavior of Indian corporate firms over the period 1990 – 2001 and attempts to explain the observed behavior with the help of trade-off theory, and signaling hypothesis. Analysis of dividend trends for a large sample of stocks traded on the NSE and BSE indicate that the percentage of companies paying dividends has declined from 60.5 percent in 1990 to 32.1 percent in 2001 and that only a few firms have consistently paid the same levels of dividends. Further, dividend-paying companies are more profitable, large in size and growth doesn't seem to deter Indian firms from paying higher dividends. Analysis of influence of changes in tax regime on dividend behavior shows that the trade off or tax-preference theory does not appear to hold true in the Indian context. Test of signaling hypothesis reinforces the earlier findings that dividend omissions have information content about future earnings. However, analysis of other non-extreme dividend events such as dividend reductions and non-reductions shows that current losses are an important determinant of dividend reductions for firms with established track record and that the incidence of dividend reduction is much more severe in the case of Indian firms compared to that of firms traded on the NYSE. Further, dividend changes appear to signal contemporaneous and lagged earnings performance rather than the future earnings performance.

Keywords: Dividend, Behaviour, Firm, Manufacturing.

Introduction:

A Dividend policy is the method by which a company structures its dividend payout to shareholders. In theory, some researchers argue that dividend policies are irrelevant because investors can sell a portion of their shares or portfolio if they need money. The dividend irrelevance theory holds that dividend payouts have little effect on a stock's price.

Regardless of whether the dividend policy is irrelevant, it is income for shareholders. Company executives are frequently the largest shareholders and stand to benefit the most from a generous dividend policy.

Most businesses consider dividend policies to be an essential component of their overall business strategy. Management must make decisions on dividend amount, timing, and a variety of other factors that affect dividend payments. Dividend policies are classified into three types: stable dividend policies, constant dividend policies, and residual dividend policies.

For a long time, corporate dividend policy has been a source of concern in financial literature. Lintner's (1956) classic work sparked the dividend debate. Despite extensive research, dividend remains a "puzzle with pieces that don't fit together" (Black, 1996). A substantial amount of research has been conducted on dividend policy, and various theories such as the theory of dividend irrelevance, signalling theory, agency cost theory, and bird in the hand theory have emerged to answer various dividend policy questions. With the publication of a seminal paper by Miller and Modigliani in 1961, the focus of research on corporate dividend policy shifted dramatically. They proposed the dividend irrelevance theory, contending that "... given a firm's investment policy, the dividend pay-out policy it chooses to follow will affect neither the current price of its shares nor the total returns to shareholders." The irrelevance theory is based on the following assumptions: (1) dividends and capital gains are taxed at the same rate, (2) there are no transaction or floatation costs when buying and selling securities, (3) all market participants have free and equal access to information, (4) there are no agency costs,

and (5) all market participants are price takers (Miller & Modigliani, 1961). Subsequent research (for example, Black and Scholes 1974; Merton and Myron 1982; Miller 1986, Bernstein 1996) mostly supported the dividend irrelevance theory.
However, managers, analysts, and investors are concerned and devote more time to dividend policy, indicating that it is important (Dennis and Stepanyan, 2009). This belief motivated the researchers to investigate the relevance of dividend policy by loosening the perfect market assumptions of irrelevance theory, which included taxes, agency problems, and information signalling, among other things. According to signalling theory, a firm will generally ensure that an increase in dividends occurs only when such an increase is certain to be associated with a higher level of future cash flows. Investors in such a firm will carefully consider the firm's competence to assess the likelihood of a high future cash flow. A company can maintain its credibility by avoiding any unexpected changes in dividend payments. An increase in dividends signals to shareholders that the company will be able to generate significant future cash flows. Pettit (1972) proposed that capital markets consider dividend announcements as information for determining share price.

Types of Dividend Policies:

Stable Dividend Policy
A stable dividend policy is the most simple and widely used. The policy's goal is to provide a consistent and predictable dividend payout each year, which is what most investors seek. Investors receive a dividend whether earnings are up or down.

Constant Dividend Policy
The main disadvantage of the stable dividend policy is that investors may not see dividend increases during boom years. A company with a constant dividend policy pays out a percentage of its earnings as dividends every year. This exposes investors to the full range of earnings volatility.

Residual Dividend Policy
Residual dividend policy is also volatile, but some investors believe it is the only acceptable dividend policy. With a residual dividend policy, the company pays out any remaining dividends after paying for capital expenditures (CAPEX) and working capital.

Factors Influencing Dividend Policy:
Many factors influence a company’s dividend policy, including:

1. Legal Restrictions: The legal restrictions that influence dividend policy are as follows:
- Dividends can only be paid out of profit and not out of capital
- Companies can declare and pay dividends using the previous year’s profit
- At least 10% of profit must be transferred to the company’s reserves

2. Size of Earnings: Dividend policy is determined by the firm's earnings. Dividend policy is influenced not only by the amount of the dividend but also by the nature of the earnings. A consistent dividend policy is preferable.

3. Shareholder Preferences: Management should pursue a policy that is beneficial to both the company and its shareholders. A consistent dividend policy is preferable.

4. Liquidity Position: The dividend policy of a company must take into account the company's liquidity position. The payment of dividends depletes the company's cash reserves.
5. Management Attitude: Because issuing new shares would change the company's control, some companies use internal sources to finance expansion programmes. Debentures issued to finance expansion run the risk of causing existing members' earnings to fluctuate.

6. Condition of Capital Market: When the capital market is stable, companies can adopt a generous dividend policy.

Review of Literature:

1. (Brahmaiah Bezawada, 2017): The relevance of dividend policies has been extensively researched, but the findings have produced little consensus. There are numerous factors that influence a given firm's dividend policy that can be found in the literature, such as the firm's risk, cash flow situation, agency costs, and so on. According to Bhattacharya (1979), a firm's dividend decision can be viewed as a source of signal, indicating that profitable firms with good project investment opportunities will pay higher dividends to differentiate themselves from other firms with projects with lower profits. This paper investigates whether a firm's dividend

policy affects its market value and the wealth of its shareholders. Our goal is to determine the impact of dividend policy on shareholder wealth in the Indian electrical equipment manufacturing industry.
2. (Geetanjali Pinto, 2019): The purpose of this research is to determine whether a company's dividends are influenced by the industry to which it belongs. This paper also investigates the explanatory factors for dividends in India's various sectors. From 2006 to 2017, this longitudinal study used balanced data from companies listed on India's National Stock Exchange (NSE).

Research Gap:

From the Research papers, articles, books reviewed by the researcher, which has paved a way for identifying the following research gap. Earlier literature focussed on non-linear relationship between share market value and dividend yields, risk perspective of dividend perceived by investor, cost minimization dividend model, firm's ownership structure and dividend policy, consistency of Dividends, Linter's model to test for dividend stability dividend-paying firm managers listed on India's National Stock Exchange (NSE) to learn about the factors influencing dividend policy, determinants of equity dividend in the Indian information technology sector. impact of group affiliation on the dividend payment decision, irrelevancy of dividend in perfect markets, cross-sectional trends in dividends at the aggregate level, Lintner's Dividend Model, valuation revisions in the aftermath of divined & so on. Un attempted area of dividend policy is industry specific dividend policy which has not been examined particularly manufacturing industry. Therefore, researcher wants to examine the manufacturing sector dividend policies across different industry through study **entitled "A Study on Dividend Policy of Listed Manufacturing Companies in India".**

Need for the study:

Despite numerous researches have been conducted, the relationship between dividend policy and market value of the firm seems to be an unresolved area. As firms face a dilemma whether its dividend pay-out criterion affects its market value, this study tries to fill in the void and establishes whether there is relationship between the dividend policy and growth in the market value among the chosen companies in the manufacturing sector of India. Dividend Policy explains about retention proportion of the Company which needs to be carefully examined. The retention Policy is will affect the Market Value of the firm. Hence, it is directly linked to the growth rate.

Proposed objective:

1) To examine dividend policy followed by the Indian manufacturing sector in terms of retention & distribution of profit.
2) To examine the difference in the dividend policy adopted by the different industry of the manufacturing sector.
3) To analyse the trends in Market Value of the chosen companies in the manufacturing sector
4) To examine the impact of dividend policy on the Market Value of the chosen companies in the manufacturing sector.
5) Designing the appropriate model to the chosen industries across the manufacturing sector with respect to ideal dividend policy to be followed.

Hypotheses:

The researcher has set the following hypotheses to fulfil the objectives of the current study.
H_{01}: Dividend distribution does not vary across the companies in the same industry
H_{02}: Dividend paid & retention ratio has no significant impact on market capitalisation
H_{03}: Homoscedasticity in dividend distribution is found across the Industry in the manufacturing sector.

Research Methodology

The study follows "Analytical and Descriptive research" methodology Descriptive research is a quantitative research method that attempts to collect quantifiable information for statistical analysis of the population sample. It is a popular research tool that allows us to collect and describe the phenomena. Analytical research is a specific type of research that involves critical thinking skills and. the evaluation of facts and information relative to the research being conducted.
In the current study Descriptive research is used to describe the dividend distribution pattern followed by different companies under different manufacturing industries. Uniformity or diversity in the dividend distribution & retention proportion of the companies in the industries are explained through descriptive research.

The study is also analytical in nature, hence it examines causal relationship between dividend policy, enterprise value & market capitalization. Incline or decline in the market capitalization is examined throughout the business cycle for a given change in the dividend distribution.

Sampling technique:

The study follows stratified systematic sampling technique, to collect the data. The researcher intends to collect the data pertaining to Capital structure, WACC, Dividend policy, Market Capitalisation from 50 companies which represent 5 industries from manufacturing sector. To have equal representation, companies were chosen on the basis of market capitalisation ranging from large cap to small cap. industries chosen for the study is as follows.

Manufacturing Industry chosen for the study	
1.	Automobile industry
2.	Iron & Steel Industry
3.	Pharmaceutical & Health Care Industry
4.	Durable consumer goods Industry
5.	FMCG Industry

Sources of Data Collection:

To analyse the trend in Capital structure, Revenue from operation, WACC, Dividend policy & Market Capitalisation uses primary data, which is collected from annual reports of selected companies for the reference period commencing from FY 2014 to 2021. 8 years of time span would be sufficient to examine the trend in the above parameters & to assess its interrelationship.
As per the Ministry of corporate affairs (MCA), notified IND AS, it is mandatory to furnish the information such as statement of changes in the equity, non-current liabilities, EVA (IND AS 1- Presentation of financial statements), in the annual reports of the company. Enterprise value & market capitalisation is also need to be supplemented in the annual report.
Such an authentic data will be gathered & compiled for the purpose of analysis of data.

Data Analysis Tools:

The researcher will be using various statistical technique such as ANOVA, Multiple regression based predictive analysis model F test Descriptive statistics tools etc. which are explained below.
ANOVA is a statistical method for defining the presence of variances among numerous population means. To examine whether the Dividend distribution remained uniform or different across the companies chosen for the study. ANOVA assumed to be an ideal tool. Hence the researcher has used ANOVA.
The researcher has used Panel Data analysis in analysing the impact of, dividend paid on market capitalisation and enterprise value.

Scope of the study:

The scope recognizes the borders of the study in term of topics, objectives, facilities, area, time frame, and the issues to which the research is focused. The study aims at analysing the trend in the capital structure, market capitalisation & enterprise value across the selected manufacturing industry.
The study aims at examining the impact of Dividend policy on market capitalisation of selected manufacturing industry of India. For this purpose 50 listed manufacturing companies has been chosen.

ANALYSIS OF AUTO MOBILE INDUSTRY

Table 1: Showing: Dividend Policy Components & its Impact on Market Capitalisation & Enterprise Value of Bajaj Auto Ltd.

(Rs, in Crore)

Year	Revenue From Operation	Net Profit	Dividend	Dividend Payout Ratio Net Profit %	Cash Earnings Retention Ratio (%)	Enterprise Value	Long Term Liabilities	Market Capital
Mar-13	19,488.96	2,813.74	144.68	39.12	59.41	51,451.43	71.27	51,380.16
Mar-14	19,717.64	3,043.57	1,302.15	37.13	57.74	59,702.03	57.74	59,644.29
Mar-15	21,103.93	3,243.32	1,446.84	102.12	53.05	57,901.68	111.77	57,789.91
Mar-16	21,373.52	3,827.56	1,446.84	102.12	31.71	68,765.80	111.77	68,654.03
Mar-17	22,151.71	3,929.67	2,893.68	80.71	96.51	81,066.85	119.9	80,946.95
Mar-18	22,151,74	3,938.00	1,820.00	39.12	63.69	78,887.69	120.77	78,766.92
Mar-19	27,132.90	4,554.59	1,736.20	37.13	64.87	83,429.99	119.9	83,310.09
Mar-20	29,111.54	4,675.18	5,208.60	102.12	2.58	58,286.26	120.77	58,165.49

Mar-21	29,567.25	5,018.87	5,208.60	102.12	2.58	105,720.62	119.9	105,600.72
Mar-22	32,135.98	5,099.98	4,051.14	80.71	23.4	105,104.05	120.77	104,983.28
Average	22,178.34	4,014.45	2,525.87	72.24	45.55	75,031.64	107.46	74,924.18
Maximum	32,135.98	5,099.98	5,208.60	102.12	96.51	105,720.62	120.77	105,600.72
Minimum	19,488.96	2,813.74	144.68	37.13	2.58	51,451.43	57.74	51,380.16
σ	4,832.25	812.57	1,747.18	30.50	29.95	19,356.64	23.13	24.13
CV	22%	20%	69%	42%	66%	26%	22%	0%
CAGR	5%	6%	40%	8%	-9%	7%	5%	7%
(Compiled from Annual Reports of Bajaj auto ltd)								

Based on the provided data on Bajaj Auto Ltd., we can analyse the impact of various components of the dividend policy on market capitalization (MC) and enterprise value (EV). Following shows the relationship between these variables:

Revenue from Operation (RO): The average revenue from operation is Rs. 22,178.34 crore, with a minimum of Rs. 19,488.96 crore and a maximum of Rs. 32,135.98 crore. There is a positive correlation between revenue and both market capitalization and enterprise value. Generally, as revenue increases, market capitalization and enterprise value tend to rise.

Net Profit (NP): The average net profit is Rs. 4,014.45 crore, with a minimum of Rs. 2,813.74 crore and a maximum of Rs. 5,099.98 crore. Similar to revenue, there is a positive correlation between net profit and both market capitalization and enterprise value. Higher net profits usually lead to increased market capitalization and enterprise value.

Dividend: The average dividend is Rs. 2,525.87 crore, with a minimum of Rs. 144.68 crore and a maximum of Rs. 5,208.60 crore. Dividends can have a mixed impact on market capitalization and enterprise value. While paying higher dividends may attract investors and increase market capitalization in the short term, it can reduce the retained earnings used for reinvestment, potentially affecting long-term enterprise value.

Dividend Payout Ratio: The average dividend pay-out ratio is 72.24%, with a minimum of 37.13% and a maximum of 102.12%. The dividend pay-out ratio represents the proportion of net profit distributed as dividends. A higher pay-out ratio indicates more dividends are being distributed, which can impact market capitalization positively but may limit the retained earnings available for reinvestment, potentially affecting enterprise value.

Cash Earnings Retention Ratio: The average retention ratio is 45.55%, with a minimum of 2.58% and a maximum of 96.51%. The retention ratio indicates the percentage of cash earnings retained by the company for reinvestment or future growth. A higher retention ratio suggests a focus on reinvestment, which can contribute to long-term enterprise value growth.

Long-Term Liabilities (LTL): The average long-term liabilities are Rs. 75,031.64 crore, with a minimum of Rs. 51,451.43 crore and a maximum of Rs. 1,05,720.62 crore. The level of long-term liabilities can influence enterprise value. Higher long-term liabilities may increase financial risk and impact enterprise value negatively.

Market Capitalization (MC) and Enterprise Value (EV): MC represents the total market value of the company's outstanding shares, while EV represents the total value of the company, including debt and the average MC is Rs. 74,924.18 crore, with a standard deviation of Rs. 19,343.42 crore. The average EV is not directly provided in the table but can be calculated using the given long-term liabilities data.
revenue from operation and net profit generally have a positive impact on both market capitalization and enterprise value. Dividend pay outs can positively affect market capitalization in the short term but may limit retained earnings for reinvestment and potentially impact long-term enterprise value. The cash earnings retention ratio is crucial for sustaining and growing enterprise value. Long-term liabilities can impact enterprise value, with higher liabilities potentially increasing financial risk.
Based on the available data, it's difficult to establish a direct relationship between the dividend policy components and MC/EV. However, it can be observed that Bajaj Auto Ltd. has shown consistent revenue growth, net profit growth, and an increasing trend in dividend payments. These factors, along with other financial indicators, contribute to the overall valuation of the company. To gain a deeper understanding, further analysis and examination of other factors affecting MC and EV would be necessary.

Table 2: Showing: Dividend Policy Components & its Impact on Market Capitalization & Enterprise Value of Atul Auto mobiles Ltd.

Rs. In Crore

Year	Revenue from operation	Net profit	Dividend	Dividend Payout Ratio Net Profit %	Cash Earnings Retention Ratio (%)	Enterprise value	Long Term Liabilities	Market capital
Mar-13	362.86	25.92	6.58	20.19	78.32	127.75	15	127.75
Mar-14	429.26	29.8	8.23	21.68	76.5	357.82	64.29	357.82
Mar-15	490.07	40.57	10.97	11.5	76.23	1,217.46	15	1,217.46
Mar-16	528.01	47.4	11.52	21.68	78.14	1,150.87	64.29	1,150.87
Mar-17	472.2	37.32	11.52	11.5	72.79	978.49	15	978.49
Mar-18	551.22	46.19	9.33	20.19	81.88	951.04	64.29	951.04
Mar-19	661.35	53.12	11.52	21.68	80.36	738.07	15	738.07
Mar-20	625.34	52.39	6.03	11.5	89.75	307.98	64.29	307.98
Mar-21	295.9	10.20	11.52	21.68	80.36	399.25	15	384.25
Mar-22	293.82	24.87	6.03	11.5	89.75	430.01	64.29	365.72
Average	471.003	36.778	9.325	17.31	80.408	665.874	39.645	657.945
Maximum	661.35	53.12	11.52	21.68	89.75	1217.46	64.29	1217.46
Minimum	293.82	10.2	6.03	11.5	72.79	127.75	15	127.75
σ	127.18	13.91	2.41	5.03	5.547	389.16	25.97	395.11
CV	27%	38%	26%	29%	7%	58%	66%	60%
CAGR	-2%	0%	-1%	-5%	1%	13%	16%	11%

Compiled from Annual Reports of the company Atul Automobile Ltd.

Based on the provided data on Atul Auto mobiles Ltd., we can analyse the impact of different dividend policy components on market capitalization (MC) and enterprise value (EV). Here are some key observations:

Revenue from Operation (RO): The average revenue from operation over the years is Rs. 471.003 crore. However, the revenue fluctuates between a minimum of Rs. 293.82 crore and a maximum of Rs. 661.35 crore. The standard deviation is 127.18914 crore, indicating a significant variation in revenue. The compound annual growth rate (CAGR) for revenue is -2%.

Net Profit (NP): The average net profit is Rs. 36.778 crore, with a minimum of Rs. 10.2 crore and a maximum of Rs. 53.12 crore. The standard deviation is 13.91107 crore. The CAGR for net profit is 0%.

Dividend and Dividend Payout Ratio: The average dividend paid by the company is Rs. 9.325 crore. The dividend pay-out ratio (dividend/net profit) averages at 17.31%. The minimum and maximum dividend pay-out ratios are 11.5% and 21.68% respectively. The standard deviation for the dividend pay-out ratio is 5.0332318%. It's important to note that the dividend pay-out ratio represents the proportion of net profit distributed as dividends to shareholders.

Cash Earnings Retention Ratio: The average cash earnings retention ratio is 80.408%, indicating that the company retains around 80% of its cash earnings for reinvestment or other purposes. The minimum and maximum retention ratios are 72.79% and 89.75% respectively. This ratio represents the percentage of cash earnings retained by the company.

Long-Term Liabilities (LTL): The company's long-term liabilities average at Rs. 39.645 crore, with a minimum of Rs. 15 crore and a maximum of Rs. 64.29 crore. The standard deviation is 25.97811 crore.

Market Capitalization (MC): The market capitalization of Atul Auto mobiles Ltd. ranges from a minimum of Rs. 127.75 crore to a maximum of Rs. 1217.46 crore. The average market capitalization is Rs. 657.945 crore, with a standard deviation of 395.1184831 crore. The compound annual growth rate (CAGR) for market capitalization is 11%.

Enterprise Value (EV): The enterprise value of the company varies between a minimum of Rs. 127.75 crore and a maximum of Rs. 1217.46 crore. The average enterprise value is Rs. 665.874 crore, with a standard deviation of 389.1603 crore. The CAGR for enterprise value is 16%.

According to the impact analysis and descriptive statistics, Atul Auto Mobiles Ltd.'s market capitalization and enterprise value may be affected in different ways by changes in revenue, stable net profit, dividend policy components, cash earnings retention ratio, and long-term liabilities. To fully comprehend how these

characteristics relate to the company's valuation, additional research and consideration of other elements are required.
Based on these statistics, we can see that the dividend policy components, such as dividend payout ratio and cash earnings retention ratio, along with other financial factors, have an impact on the market capitalization and enterprise value of Atul Auto mobiles Ltd.

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