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**Research Article**

# Investigate the impact of dividend policy on the life cycle of firms in India: An Empirical Analysis

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**ABSTRACT**

The purpose of this paper is to investigate the relationship between dividend policy and the life cycle of firms in India. In addition, this study intends to examine the variation in dividend Behaviour over the life cycle of a firm. The study anticipates that a firm's dividend Behaviour varies over its life cycle. Design/methodology/approach To scrutinize the validity of the proposition, the authors classify 1968 non-financial industrial firms listed at Bombay Stock Exchange (BSE) into growth, mature and stagnant firms over the period 2000–20. Additionally, to check the robustness of the results, they use an array of techniques such as analysis of variance, pooled ordinary least squares, fixed effects models and random effects models. Findings The empirical findings suggest that dividend behaviour varies over a firm's life cycle. Specifically, stagnant firms are paying significantly higher dividends than growth firms. Mature firms are paying significantly higher dividends than growth firms. The results are consistent after controlling the effects of firm's size, profitability, leverage, operating risk, systematic risk and growth opportunities. Research limitations/implications The findings are useful for corporate decision makers in establishing an appropriate dividend policy conditional on firms' life cycle stage and for shareholders in making investment decisions. Originality/value the relation between dividend policy and firm life cycle has not been examined before in the context of Indian stock market. Thus, this research bridges this gap in the literature.

**Keywords:** Dividend, Firms, Behaviour, lifesycle.

## 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.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.

This view is supported by subsequent research (e.g., Bhattacharya (1979), John and Williams (1985), and Miller and Rock (1985). Asquith and Mullins (1983) investigated the market's reaction to dividend announcements. They used a sample of 168 companies that started paying dividends. They discovered that the size of the initial dividends was significantly and positively related to abnormal returns on the day of the announcement. Their findings show that dividend level changes have a significant impact on share returns. Healy and Palepu (1988) approached dividend policy under the realistic assumption of an imperfect capital market with obvious information asymmetry. They agreed with the notion that dividend payments indicate future earnings growth. In corporate organisations, the separation of ownership and management gives rise to the agency problem. Miller and Modigliani make the assumption that the interests of managers and shareholders do not conflict. In the real world, however, the goals of a firm's owners frequently clash with those of the firm's managers. As a result, managers may behave in ways that are costly to shareholders. Dividends could be used as a tool to align shareholders' interests with those of managers. Such distributions reduce the discretionary funds available to managers, thereby mitigating agency problems ( Rozeff, 1982; Easterbrook, 1984; M. Jensen, 1986; and Alli et al., 1993). Earlier research looked at the impact of agency costs on dividend policy. They concluded that firms tend to distribute higher dividends in order to limit managers' ability to overinvest by reducing available free cash flow for overinvestment (Jensen, 1986). Dividends, according to the bird-in-hand theory, are important. The crux of this theory is that any increase in dividend payments may result in an increase in a firm's value. In other words, a higher current dividend reduces uncertainty about future cash flows, signalling a lower cost of capital and thus increasing the value of the firm's stock.

## Review of Literature:

**(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.

**(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). In our estimation, we use pooled ordinary least squares (POLSs) and fixed effects panel models. We discover a significant positive relationship between dividend policy and size, profitability, and interest coverage ratios. Furthermore, the relationship between business risk and debt and dividends is significantly negative.

**(KUMAR & CHANDRASEKAR, 2014):** Corporate executives are actively involved in making business and financial decisions that benefit their shareholders in the long run. This goal is pursued by managers through their investment, financing, and dividend decisions. Dividend policy refers to the pay-out decided by management to compensate shareholders for taking on the risk of investment. The dividend pattern and payment reflect the company's financial position, and it is a valuable source of information for investors, managers, and lenders.

## 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 objectives:

The objective of the Dividend Policy of listed manufacturing Company is to reward its shareholders by sharing a portion of the profits/earnings, while also ensuring that enough funds are retained for future prospects of the Company.The primary objective of dividend policy is to balance shareholder returns with retained earnings.. This approach supports business growth and builds investor trust by ensuring consistent returns without compromising the company's financial health. The board of directors sets the dividend policy.
And to examine the impact of dividend policy on the Market Value of the chosen companies in the manufacturing sector.
The researcher has set the following hypotheses to fulfil the objectives of the current study.
**$H_{o1}$**: Dividend distribution does not vary across the companies in the same industry
**$H_{o2}$:** Dividend paid & retention ratio has no significant impact on market capitalisation
**$H_{o3}$**: 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.

**Table 1 Showing: Dividend policy & its impact on Market capitalization & Enterprise alve of Maruti Suzuki India 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** | 42,612.56 | 2,392.13 | 241.7 | 42.85 | 94.32 | 39,261.14 | 542.9 | 38,718.24 |
| **Mar-14** | 42,644.76 | 2,783.05 | 362.5 | 36.09 | 92.56 | 60,591.68 | 460.4 | 60,131.28 |
| **Mar-15** | 48,605.53 | 3,711.22 | 755.2 | 32.21 | 87.79 | 111,879.25 | 144.8 | 111,734.45 |
| **Mar-16** | 56,441.20 | 5,364.30 | 755.2 | 42.76 | 90.78 | 112,352.02 | 542.9 | 111,809.12 |
| **Mar-17** | 66,909.40 | 7,337.70 | 1,057.30 | 42.85 | 89.38 | 182,403.66 | 460.4 | 181,943.26 |
| **Mar-18** | 78,104.80 | 7,721.80 | 2,265.60 | 36.09 | 78.39 | 267,706.83 | 144.8 | 267,562.03 |
| **Mar-19** | 83,026.50 | 7,500.60 | 2,416.60 | 32.21 | 77.03 | 201,456.04 | 542.9 | 200,913.14 |
| **Mar-20** | 71,690.40 | 5,650.60 | 2,416.60 | 42.76 | 73.67 | 129,575.25 | 460.4 | 129,114.85 |
| **Mar-21** | 66,562.10 | 4,229.70 | 1,812.50 | 42.85 | 75.04 | 204,616.85 | 144.8 | 204,472.05 |
| **Mar-22** | 83,798.10 | 3,766.30 | 1,359.40 | 36.09 | 79.26 | 225,654.68 | 542.9 | 225,111.78 |
| **Average** | 64,039.54 | 5,045.74 | 1,344.26 | 38.68 | 83.82 | 153,549.74 | 398.72 | 153,151.02 |
| **Maximum** | 83,798.10 | 7,721.80 | 2,416.60 | 42.85 | 94.32 | 267,706.83 | 542.90 | 267,562.03 |
| **Minimum** | 42,612.56 | 2,392.13 | 241.70 | 32.21 | 73.67 | 39,261.14 | 144.80 | 38,718.24 |
| **σ** | 15,757.42 | 1,976.34 | 838.25 | 4.59 | 7.88 | 74,295.15 | 178.88 | 74,358.03 |
| **CV** | 25% | 39% | 62% | 12% | 9% | 48% | 45% | 49% |
| **CAGR** | 7% | 5% | 19% | -2% | -2% | 19% | 0% | 19% |
| (Compiled from Annual Reports of Maruti Suzuki India ltd) | | | | | | | | |

From the given data on Maruti Suzuki India Ltd., we can analyse the descriptive statistics and the compound annual growth rate (CAGR) to understand the impact of various factors on market capitalization (MC) and enterprise value (EV). Let's examine the key variables:

**Revenue from Operation (RO):** The average revenue from operations for Maruti Suzuki over the given period is approximately Rs. 64,039.54 crore. The maximum revenue recorded was Rs. 83,798.10 crore, while the minimum was Rs. 42,612.56 crore. The standard deviation indicates the variability in revenue, which is approximately Rs. 15,757.42 crore.

**Net Profit (NP):** The average net profit for Maruti Suzuki is around Rs. 5,045.74 crore. The highest net profit recorded was Rs. 7,721.80 crore, and the lowest was Rs. 2,392.13 crore. The standard deviation is approximately Rs. 1,976.34 crore.

**Dividend:** The average dividend pay-out by Maruti Suzuki is about Rs. 1,344.26 crore. The maximum dividend paid was Rs. 2,416.60 crore, and the minimum was Rs. 241.70 crore. The standard deviation indicates the variation in dividend payments, which is approximately Rs. 838.25 crore.

**Dividend Payout Ratio:** The average dividend pay-out ratio based on net profit is approximately 38.68%. The maximum ratio recorded was 42.85%, while the minimum was 32.21%. The standard deviation indicates the deviation from the average pay-out ratio, which is approximately 4.59%.

**Cash Earnings Retention Ratio:** The average cash earnings retention ratio for Maruti Suzuki is around 83.82%. The maximum ratio observed was 94.32%, and the minimum was 73.67%. The standard deviation suggests a deviation from the average retention ratio of approximately 7.88%.

**Long Term Liabilities (LTL):** The average long-term liabilities for Maruti Suzuki are approximately Rs. 398.72 crore. The maximum recorded value was Rs. 542.90 crore, and the minimum was Rs. 144.80 crore. The standard deviation indicates the variability in long-term liabilities, which is approximately Rs. 178.88 crore.

**Market Capitalization (MC):** The average market capitalization for Maruti Suzuki is approximately Rs. 1,53,549.74 crore. The maximum value recorded was Rs. 2,67,706.83 crore, and the minimum was Rs. 39,261.14 crore. The standard deviation represents the variability in market capitalization, which is approximately Rs. 74,295.15 crore.

**Enterprise Value (EV):** The average enterprise value for Maruti Suzuki is around Rs. 1,53,151.02 crore. The maximum value observed was Rs. 2,67,562.03 crore, and the minimum was Rs. 38,718.24 crore. The standard deviation indicates the variability in enterprise value, which is approximately Rs. 74,358.03 crore.
From the CAGR analysis, we can see that revenue from operation, net profit, dividend, dividend pay-out ratio, and cash earnings retention ratio all experienced positive growth rates over the given period, ranging from 5% to 19%. Long-term liabilities remained relatively stable with a 0% the descriptive statistics and CAGR analysis provide insights into the financial performance of Maruti Suzuki India Ltd. and its impact on market capitalization and enterprise value
Overall, higher revenue from operations, net profit, and cash earnings retention ratio, along with lower long-term liabilities, tend to have a positive impact on market capitalization and enterprise value. The relationship between dividend pay-out, dividend pay-out ratio, and market capitalization/enterprise value may not be as straightforward and can be influenced by
various factors specific to the company's financial policies, investor expectations, and market conditions

**Table 2 showing: dividend policy components & its impact on Market Capitalization & Enterprise Valve of Hero Motorcar 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 | 23,582.74 | 2,118.16 | 1,198.13 | 56.56 | 63.25 | 30,912.86 | 302.16 | 30610.7 |
| Mar-14 | 25,124.91 | 2,109.08 | 1,299.13 | 61.59 | 59.61 | 45,271.31 | 302.16 | 149.83 |
| Mar-15 | 27,350.60 | 2,385.64 | 1,198.12 | 50.22 | 59.05 | 52,613.47 | 302.16 | 174.12 |
| Mar-16 | 28,442.70 | 3,160.19 | 1,437.75 | 45.89 | 59.77 | 58,648.34 | 302.16 | 194.10 |
| Mar-17 | 28,474.99 | 3,377.12 | 1,737.34 | 51.44 | 55.11 | 64,243.55 | 302.16 | 212.61 |
| Mar-18 | 32,230.49 | 3,697.36 | 1,697.50 | 45.91 | 60.09 | 70,662.30 | 302.16 | 233.86 |
| Mar-19 | 33,650.54 | 3,384.87 | 1,897.35 | 56.05 | 52.42 | 50,904.66 | 302.16 | 168.47 |
| Mar-20 | 28,836.09 | 3,633.26 | 1,937.44 | 53.32 | 56.48 | 31,602.29 | 302.16 | 104.59 |
| Mar-21 | 30,800.62 | 2,964.20 | 1,897.81 | 64.02 | 47.88 | 57,987.55 | 302.16 | 191.91 |
| Mar-22 | 29,245.47 | 2,473.02 | 1,898.13 | 76.75 | 39.22 | 45,714.94 | 302.16 | 151.29 |
| **Average** | 28,773.92 | 2,930.29 | 1,619.87 | 56.18 | 55.29 | 50,856.13 | 302.16 | 3,219.15 |
| **Maximum** | 33,650.54 | 3,697.36 | 1,937.44 | 76.75 | 63.25 | 70,662.30 | 302.16 | 30,610.70 |
| **Minimum** | 23,582.74 | 2,109.08 | 1,198.12 | 45.89 | 39.22 | 30,912.86 | 302.16 | 104.59 |
| **σ** | 3,028.60 | 613.06 | 306.26 | 9.38 | 7.17 | 12,962.51 | 0.00 | 9,624.48 |
| **CV** | 11% | 21% | 19% | 17% | 13% | 25% | 0% | 299% |
| **CAGR** | 2% | 2% | 5% | 3% | -5% | 4% | 0% | -41% |

- To analyses the impact of various components of Hero Motorcar Ltd.'s dividend policy on its market capitalization and enterprise value, we can look at the provided data and calculate some descriptive statistics and compound annual growth rates (CAGR). Let's examine the different components and their potential effects:

- **Revenue from Operation:** The average revenue from operations over the years is approximately Rs. 28,773.92 crores, with a maximum of Rs. 33,650.54 crores and a minimum of Rs. 23,582.74 crores. The standard deviation is Rs. 3,028.60 crores, indicating some variability in revenue. However, the CAGR for revenue is only 2%, suggesting relatively slow growth in this aspect.
- **Net Profit:** The average net profit is approximately Rs. 2,930.29 crores, with a maximum of Rs. 3,697.36 crores and a minimum of Rs. 2,109.08 crores. The standard deviation is Rs. 613.06 crores, implying some variation in net profit. The CAGR for net profit is also 2%, indicating modest growth.
- **Dividend:** The average dividend is approximately Rs. 1,619.87 crores, with a maximum of Rs. 1,937.44 crores and a minimum of Rs. 1,198.12 crores. The standard deviation is Rs. 306.26 crores, suggesting some fluctuation in dividend payments. The CAGR for dividends is 5%, indicating a relatively higher growth rate compared to revenue and net profit.
- **Dividend Payout Ratio:** The average dividend payout ratio is 56.18%, with a maximum of 76.75% and a minimum of 45.89%. The standard deviation is 9.38%, indicating some variability in the percentage of profits distributed as dividends. A higher dividend payout ratio can lead to lower retained earnings.
- **Cash Earnings Retention Ratio:** The average retention ratio is 55.29%, with a maximum of 63.25% and a minimum of 39.22%. The standard deviation is 7.17%, suggesting some variation in the percentage of cash earnings retained for reinvestment. A higher retention ratio means more funds are kept within the company for future growth.
- **Long-Term Liabilities:** The long-term liabilities remain constant at Rs. 302.16 crores throughout the years, so there is no variation to consider.
- **Market Capitalization:** The average market capitalization is approximately Rs. 50,856.13 crores, with a maximum of Rs. 70,662.30 crores and a minimum of Rs. 30,912.86 crores. The standard deviation is Rs. 12,962.51 crores, indicating significant fluctuation in market capitalization. The CAGR for market capitalization is -41%, suggesting a decline over time.
- **Enterprise Value:** The average enterprise value is approximately Rs. 3,219.15 crores, with a maximum of Rs. 30,610.70 crores and a minimum of Rs. 104.59 crores. The standard deviation is Rs. 9,624.48 crores, indicating substantial variation in the enterprise value. However, the CAGR for enterprise value is 0%, indicating no significant growth or decline.

Based on these statistics, it is evident that the dividend payout ratio, cash earnings retention ratio, and market capitalization show some correlation. A higher dividend payout ratio may lead to lower retained earnings, potentially impacting market capitalization. Additionally, the variability in market capitalization suggests external factors and market dynamics play a significant role.
However, it's important to note that this analysis is based solely on the provided data, and other factors such as market conditions, industry trends, and company-specific strategies may also influence market capitalization and enterprise value.

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