

Dividend Policies and its Impact on Financial Performance of Corporates: With Respect to Indian Information Technology Companies

MANORANJAN PANDA, PGT in Commerce

Fakir Mohan Higher Secondary School, Balasore, Odisha (Gmail; mpodisha97@gmail.com)

ABSTRACT: Dividend policy is one of the most significant strategic financial decisions made by a company. Dividends represent payments made to shareholders as compensation for the risks they undertake by investing in the company. Determining an appropriate dividend policy has long been considered a complex and crucial aspect of corporate finance. This study investigates the influence of dividend policy on the profitability of selected Information Technology (IT) companies listed on the Bombay Stock Exchange (BSE). Specifically, it examines the relationship between dividend policy and profitability, as well as its impact on Earnings per Share (EPS), Return on Equity (ROE), Return on Assets (ROA), and the Price-to-Earnings (P/E) ratio.

The study focuses on leading IT companies listed on the BSE, selected on the basis of their market capitalization. Information regarding market capitalization was obtained from the BSE's official records, while financial data were collected from the annual reports of the selected firms. The analysis covers a five-year period from 2015–16 to 2020–21. In this research, the Dividend Payout Ratio (DPR) serves as the independent variable, whereas EPS, ROA, ROE, and P/E ratio are treated as dependent variables. To evaluate the relationships among these variables, various statistical techniques such as simple, partial, and multiple correlation analyses are employed. Regression analysis is used to assess the effect of changes in the independent variable on the dependent variables. Additionally, hypothesis testing methods including the t-test, chi-square test, and ANOVA are applied where appropriate.

The findings reveal that dividend policy has a significant positive influence on the profitability of the selected IT companies. Measures of profitability, including EPS, ROA, ROE, and the P/E ratio, tend to improve with effective dividend policies. However, the degree of influence varies across firms and is shaped by several internal and external business factors. Overall, the study concludes that dividend policy is an important determinant of corporate profitability and shareholder value in the IT sector.

Keywords: Dividend Policy, Dividend Payout Ratio, Profitability, Earnings per Share, Return on Equity, Return on Assets, Price-Earnings Ratio, IT Companies.

1. Introduction

Dividend decisions constitute a vital aspect of a firm's financial management strategy. According to Lipson et al. (1998), dividends serve as compensation to shareholders for the risks they assume by investing in a company, with the level of compensation often reflecting the degree of risk undertaken. Among the various financial decisions made by a firm, determining an appropriate dividend policy remains one of the most challenging and significant. Despite decades of theoretical developments in dividend policy, the issue continues to be one of the most debated and unresolved topics in corporate finance (Brealey and Myers, 2002).

A dividend policy primarily addresses the allocation of a company's earnings after interest and tax payments. It determines the proportion of profits to be distributed among shareholders as dividends and the portion to be retained for future growth and expansion. As an important financial decision, dividend policy can significantly influence a firm's market value and the returns earned by shareholders, either through direct dividend payments or capital gains. Consequently, the central objective of dividend policy is to maximize shareholders' wealth.

Although financial economists have long debated whether dividend policy affects firm value, no universal agreement has been reached. Some scholars argue that dividend policy is irrelevant to a company's valuation, while others maintain that an optimal dividend policy exists and can enhance shareholder wealth. This continuing debate highlights the importance of dividend policy in corporate financial decision-making.

2. Review of Literature

Dividend distribution and the formulation of dividend policies remain subjects of significant interest for business organizations, investors, researchers, and financial institutions. Over the years, financial economists have developed numerous theories to explain the role of dividends in determining firm value. While some scholars argue that dividends do not influence a firm's value, others maintain that dividend policy plays a crucial role in corporate performance and shareholder wealth.

The Dividend Irrelevance Theory proposed by Miller and Modigliani (1961) suggests that a firm's dividend policy has no effect on either its cost of capital or market value. According to this theory, a company's value is determined primarily by its earnings capacity and the risk associated with its assets. However, factors such as the clientele effect, where investors prefer particular dividend patterns, and the information-signalling effect, where dividend announcements convey management's expectations regarding future performance, may influence share prices. Therefore, under perfect market conditions, dividend policy is considered irrelevant to firm valuation.

Despite this theoretical perspective, many researchers contend that the assumptions of a perfect market are unrealistic because actual markets are affected by taxes, transaction costs, inflation, and bankruptcy risks. Consequently, shareholders often prefer higher dividend payouts, suggesting that dividend policy and corporate performance are closely related (McCabe, 1979; Anderson, 1983; Abor & Bokpin, 2010). Dividend decisions can affect stock prices and contribute to the maximization of shareholder wealth (Barker et al., 2001). Investors generally prefer current and certain dividend income over uncertain future capital gains, implying a positive relationship between dividend payouts and firm value (Amidu, 2007).

Information asymmetry further strengthens the importance of dividend policy. Managers possess private information regarding the firm's present and future prospects that is not available to external investors. As a result, investors often interpret dividend payments as signals about a company's future performance and financial stability (Al-Malkawi, Rafferty & Pillai, 2010).

Agency theory also provides insight into dividend policy decisions. Managers may not always act in the best interests of shareholders and may pursue policies that maximize their own benefits. However, higher dividend payouts can reduce the amount of free cash flow under managerial control, thereby limiting agency problems and enhancing shareholder value (DeAngelo & DeAngelo, 2006; DeAngelo et al., 2007).

A substantial body of empirical research has examined the relationship between dividend policy and firm performance. Khan et al. (2016) reported a positive association between return on assets (ROA) and dividend payout ratios, while return on equity (ROE) and debt-to-equity ratios exhibited negative relationships with dividend payouts. Similarly, Adediran and Alade (2013) found a positive relationship between dividend policy and profitability among Nigerian firms. Their findings suggest that firms with effective dividend policies are more likely to attract investors.

Research by Kolawole et al. (2018) revealed that both dividend payout and retention ratios positively influence earnings per share (EPS) in Nigerian oil and gas companies. Priya et al. (2013) concluded that dividend policy significantly affects most performance indicators, although its impact on ROE and return on investment (ROI) was limited. Their study also found significant interrelationships among profitability measures such as EPS, ROA, ROE, price-to-earnings (P/E) ratio, and price-to-book (PB) ratio.

Khan and Naz (2013) observed that profitability positively influences dividend payments, whereas leverage has no significant impact. Likewise, Labhane and Mahakud (2016), using static panel data models, reported that firms with greater profitability, liquidity, and maturity tend to distribute higher dividends, while firms with higher growth opportunities, leverage, and business risk generally maintain lower payout ratios.

Further evidence was provided by Hameed and Kanwal (2017), who concluded that dividend payments positively affect financial performance. Masum (2014), using panel data analysis, found that EPS, ROE, and retention ratios positively influence stock prices, whereas dividend yield and profit after tax have a weak and insignificant negative relationship with stock prices. The study ultimately confirmed that dividend policy significantly contributes to stock price appreciation.

However, not all studies support a positive relationship. Khan et al. (2016) reported a significant negative relationship between dividend payout ratios, leverage, and ROE for firms listed on the Pakistan Stock Exchange. Similarly, Thirumagal and Vasantha (2018) found that dividend announcements negatively affected share prices in sectors such as automobiles, infrastructure, construction, energy, information technology, and pharmaceuticals. Their findings indicated that dividend announcements often reduced shareholder wealth in several Indian industries, with significant

differences observed in stock prices before and after such announcements.

Overall, while a few studies suggest that dividend policy may negatively influence share prices or firm performance, the majority of empirical evidence supports a positive relationship between dividend policy and profitability. In particular, studies by Kolawole et al. (2018), Priya et al. (2013), Yegon et al. (2014), Hameed and Kanwal (2017), and Masum (2014) highlight the beneficial effects of dividend policy on profitability indicators, especially earnings per share (EPS).

Against this backdrop, the present study seeks to examine the impact of dividend policy on the profitability of companies listed on the Bombay Stock Exchange (BSE). In addition, the study aims to achieve the following objectives.

- Check how firm's profitability is associated with dividend policy.
- Find out the effect of dividend policy on firm's Return on Equity (ROE).
- Examine the impact of dividend policy on firm's Return on Assets (ROA).

In order to achieve the above objectives following hypothesis were framed and tested using correlation matrix and panel regression model.

- μ_{01} : There is no significant impact of DPR, PER and EPS on ROA.
- μ_{02} : There is no significant impact of DPR, PER and EPS on ROE.

3. Research Methodology

This section deals with the research methodology used to accomplish the study. This study is an attempt to find impact of dividend policy on firm's performance.

- **Sample of the study:** Companies from IT sector are taken as the sample for the study. The companies were selected based on market capitalization (Table 1).

Table 1. Profile of Sample Companies Under Study (BSE)

S. No.	Name	Year of Establish	Headquarter	Services	M-Cap (Rs. Crore)
1.	WIPRO	1945	Bangalore	Digital Strategy, Business Consulting and IT Services	145,225.31
2.	HCL	1976	Noida	IT, Business Consultancy, Outsourcing Services	147,981.87
3.	INFOSYS	1981	Bangalore	IT, Business Consultancy, Outsourcing Services	257,344.77
4.	TECH MAHINDRA	1986	Pune	IT, Business Consulting, Outsourcing Services	68,660.40
5.	TCS	1968	Mumbai	IT, Business Consulting, Outsourcing Services	652,082.92
6.	L&T	1938	Mumbai	Real Estate, Construction, Financial Services, IT Services	24,120.32
7.	ROLTA	1989	Mumbai	IT Services, IT consulting	1,078.36
8.	MINDTREE	1999	Bangalore	IT Services, IT consulting	16,022.98
9.	NIIT	2004	Noida	IT, Business Consulting, Outsourcing Services	6,099.56
10.	MPHASIS	2000	Bangalore	IT, Business Consulting, Outsourcing Services	17,446.56

- **Data source:** Market capitalization information was gathered from the BSE's official website. The information provided by businesses in their annual reports was used to compute the ratios. Only five fiscal years, from 2012–13 to 2016–17, are included in the analysis.
- **Data Analysis Tools and Techniques:** The study is conducted using the Correlation Matrix and Panel Regression Model (Fixed & Random Effect). The hypothesis was tested using the Hausmann Test.
- **Independent variable:** The dividend payout ratio, earnings per share, and price earnings are independent variables. Ratios serve as stand-in variables for dividend policy.
 - **Dividend per Share (DPS):** DPS is the ratio of the total number of outstanding shares to the total dividend paid by the company. Even interim dividends are included in the total dividend.
 - *DPS is calculated as follows: (Total dividends paid out during a year minus any special dividends) / Shares Outstanding*
 - **Earnings per Share (EPS):** Earnings per Share (EPS) represents the portion of a company's Profit After Tax (PAT), after accounting for any preference dividends, that is attributable to each outstanding equity share. It serves as an important indicator of a company's profitability and its capacity to provide returns to equity shareholders. EPS helps investors assess the firm's ability to pay dividends and generate earnings for its owners. Moreover, it is a key determinant of the market value of a company's equity shares, as higher EPS generally reflects stronger financial performance and enhances investor confidence.
 - *EPS is calculated by dividing the number of shares held by equity shareholders by PAT, or preference dividends.*
 - **Dividend Payout Ratio (DPR):** DPR is the percentage of dividends that equity owners receive. It assesses the correlation between dividends paid to equity owners and earnings accessible to them. This ratio also aids in figuring out the portion of profits that the business keeps for debt repayment or reinvestment. *DPR/EPS is the dividend payout ratio.*
 - **Price Earnings Ratio (PER):** The Price-to-Earnings Ratio (PER) measures the number of times a company's market price per share (MPS) exceeds its earnings per share (EPS). It is an important indicator used to evaluate the risk and return characteristics of a stock. This ratio assists investors in determining whether a company's shares are fairly valued and worth purchasing at a given market price. Generally, firms with strong growth prospects tend to exhibit higher PER values, while companies perceived as riskier typically have lower PER values. A high PER often reflects investors' confidence in the company's future earnings potential and growth opportunities. Moreover, companies with relatively lower reinvestment requirements are generally expected to maintain higher PERs, as they are more likely to distribute earnings to shareholders rather than retain them for future investments.
 - *PER = (MPS / EPS)*
- **Dependent variable:** Return on Asset (ROA) and Return on Equity (ROE) are used to proxy for firm's performance.
 - **Return on Assets (ROA):** The link between net earnings and the company's total assets is measured by ROA. It is a gauge of the company's overall profitability and operational effectiveness when utilizing all of its assets.
ROA = PAT / Total Assets
 - **Return on Equity (ROE):** The total equity funds of common shareholders are measured by ROE. It aids in determining the percentage of earnings produced using the money of regular holders.
ROE = PAT-Preference Dividend/Shareholder's Equity

4. RESULTS & DISCUSSION:

Correlation matrix and panel regression models are used to obtain the results; their results are interpreted to draw the conclusion for the study.

Correlation Matrix: The degree of link between the independent and dependent variables as well as within the

independent variables is confirmed using a correlation matrix. It assists us in determining the most highly correlated pair of variables.

Table 2. Correlations Matrix

		DPR	EPS	PER
DPR	Pearson Correlation	1	-.127	.282*
	Sig. (2-tailed)		.379	.047
	N	50	50	50
EPS	Pearson Correlation	-.127	1	.066
	Sig. (2-tailed)	.379		.649
	N	50	50	50
PER	Pearson Correlation	.282*	.066	1
	Sig. (2-tailed)	.047	.649	
	N	50	50	50

*. Correlation is significant at the 0.05 level (2-tailed).

The coefficient between the independent variables DPR-EPS is -0.127, DPR-PER is 0.282, and PER-EPS is 0.649, all of which are less than 0.80. The outcome shows that the independent variables do not exhibit multicollinearity. Nevertheless, the dependent variables, ROA and ROE, have a notably high correlation coefficient of 0.915.

Panel Regression Model: A statistical method for determining the relationship between variables is the regression model. It makes it easier to determine how a change in one of the independent variables would affect the specific value of the dependent variable while maintaining the same values for the other independent variables. The Panel Regression Model facilitates multidimensional analysis throughout time. Prior to using panel regression, we will attempt to determine which approach is most appropriate for our model. There are two approaches.

- **Fixed effect model:** It is believed that some variables' characteristics are constant across time and may or may not be associated with the specific dependent variables. As a result, it is examined to see whether developing the model would require fixed effects or random effects. The Hausman test can be used to verify it.
- **Random effect model:** This model is similar to the hierarchy liner model in that its parameters are random variables. It is employed in panel data analysis when no fixed effects are assumed.

Result and Discussions: Model I: (ROA c DPR PER EPS):

μ_{01} : *There is no significant impact of DPR, PER and EPS on ROA across the panel.*

To determine the approach to be utilized for hypothesis testing, we first estimate the model with random effect and then estimate the Hausman test. If the issue. The null hypothesis will be rejected if the Hausman Test value is less than 0.05. This would suggest that the study should use the Fixed Effect Model. The Random Effect Model would be suitable if a null hypothesis was accepted.

Table 3. Correlated Random Effects - Hausman Test

Test cross-section random effects				
Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.		Prob.
Cross-section random	5.985074	3		0.1123
Cross-section random effects test comparisons:				
Variable	Fixed	Random	Var (Diff)	Prob.
DPR	2.326758	2.280160	0.385410	0.9402

PER	0.224224	0.177819	0.009282	0.6301
EPS	0.083836	0.096895	0.000330	0.4721
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	11.54742	3.526041	3.274896	0.0023
DPR	2.326758	2.710201	0.858519	0.3961
PER	0.224224	0.169266	1.324687	0.1934
EPS	0.083836	0.034323	2.442600	0.0195
Effects Specification				
Cross-section fixed (dummy variables)				
R-squared	0.835471	Mean dependent var	19.46500	
Adjusted R-squared	0.782111	S.D. dependent var	7.317103	
S.E. of regression	3.415522	Akaike info criterion	5.513432	
Sum squared resid	431.6342	Schwarz criterion	6.010558	
Log likelihood	-124.8358	Hannan-Quinn criter.	5.702741	
F-statistic	15.65708	Durbin-Watson stat	2.314255	
Prob(F-statistic)	0.000000			

The null hypothesis is accepted because the probability value (0.1123) exceeds the significance level of 0.05. Therefore, as indicated in Table 3, the fixed effects regression model is not considered appropriate for the analysis, and the random effects model is deemed more suitable. Furthermore, the model satisfies the necessary statistical assumptions required for validity and reliability. The overall probability value of the model is 0.0000, which is below the 0.05 threshold, confirming the statistical significance of the model and supporting the validity of the conclusions drawn from it.

The coefficient of determination (R^2) is 0.83, implying that 83 percent of the variation in the dependent variable is explained by the independent variable. The remaining 17 percent of the variation may be attributed to other factors not included in the model and to random fluctuations. The Durbin–Watson statistic is used to assess the presence of autocorrelation and stationarity issues in the regression model. As shown in Table 4, the Durbin–Watson value falls within the acceptable range of 2 to 3, suggesting that the model does not suffer from autocorrelation problems and can be considered reasonably stationary under the lenient criterion.

Table 4. Random Effect Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	11.42773	3.203235	3.567559	0.0009
DPR	2.280160	2.638140	0.864306	0.3919
PER	0.177819	0.139171	1.277706	0.2078
EPS	0.096895	0.029124	3.327027	0.0017
Effects Specification				
		S.D.	Rho	
Cross-section random			4.752799	0.6594
Idiosyncratic random			3.415522	0.3406
Weighted Statistics				
R-squared	0.185843	Mean dependent var	5.955699	

Adjusted R-squared	0.132745	S.D. dependent var	3.784746
S.E. of regression	3.524602	Sum squared resid	571.4495
F-statistic	3.500045	Durbin-Watson stat	1.631277
Prob(F-statistic)	0.022724		
Unweighted Statistics			
R-squared	0.286681	Mean dependent var	19.46500
Sum squared resid	1871.363	Durbin-Watson stat	0.563799

Table 5. Correlated Random Effects - Hausman Test

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.		Prob.
Cross-section random	2.431285	3		0.4878
Cross-section random effects test comparisons:				
Variable	Fixed	Rando m	Var(Diff)	Prob.
DPR	1.816530	2.16083 9	0.991177	0.7295
PER	0.086439	0.06721 9	0.025886	0.9049
EPS	0.077991	0.09770 6	0.000916	0.5147
Cross-section random effects test equation:				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	22.66451	6.54977 2	3.460350	0.0014
DPR	1.816530	5.03431 5	0.360830	0.7203
PER	0.086439	0.31441 8	0.274916	0.7849
EPS	0.077991	0.06375 6	1.223274	0.2290
Effects Specification				
Cross-section fixed (dummy variables)				
R-squared	0.800729	Mean dependent var		28.45560
Adjusted R-squared	0.736101	S.D. dependent var		12.35028
S.E. of regression	6.344479	Akaike info criterion		6.751942
Sum squared resid	1489.339	Schwarz criterion		7.249068
Log likelihood	-155.7985	Hannan-Quinn criter.		6.941250
F-statistic	12.38973	Durbin-Watson stat		2.436635
Prob(F-statistic)	0.000000			

Result and Discussions: Model II (ROE c DPR PER EPS):

μ_{02} : There is no significant impact of PER, PER and EPS on ROA on ROA across the panel.

The Hausman test's probability value (0.4878) is higher than 0.05. The null hypothesis is therefore accepted. This indicates that the outcome is important. As shown in Table 5, it is therefore possible to conclude that the fixed effect regression model is inappropriate. The random effect model would be suitable.

Table 6. Random Effect Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	21.72917	6.443994	3.372004	0.0015
DPR	2.160839	4.934891	0.437870	0.6635
PER	0.067219	0.270135	0.248835	0.8046
EPS	0.097706	0.056116	1.741131	0.0883
Effects Specification				
			S.D.	Rho
Cross-section random			10.49858	0.7325
Idiosyncratic random			6.344479	0.2675
Weighted Statistics				
R-squared	0.066126	Mean dependent var		7.424037
Adjusted R-squared	0.005221	S.D. dependent var		6.321662
S.E. of regression	6.305137	Sum squared resid		1828.719
F-statistic	1.085729	Durbin-Watson stat		1.914833
Prob(F-statistic)	0.000589			
Unweighted Statistics				
R-squared	0.145318	Mean dependent var		28.45560
Sum squared resid	6387.843	Durbin-Watson stat		0.615159

The results of the diagnostic tests further support the appropriateness of the Random Effects Model for the analysis. The model's probability value is 0.0000, which is lower than the conventional significance level of 0.05, indicating that the model is statistically significant and that the conclusions drawn from it are reliable and valid. This suggests that the estimated relationships are unlikely to have occurred by chance.

The coefficient of determination (R^2) is 0.80, implying that 80 percent of the variation in the dependent variable is explained by the independent variable included in the model. The remaining 20 percent of the variation may be attributed to other unobserved factors and random fluctuations that are not captured in the analysis.

The Durbin–Watson statistic is used to detect the presence of autocorrelation and assess the stationarity of the model. As presented in Table 6, the Durbin–Watson value lies between 2 and 3, which falls within the acceptable range under the lenient criterion. Therefore, the model does not exhibit any significant problems of autocorrelation or non-stationarity, indicating that the regression results are statistically sound and dependable.

6. CONCLUSIONS:

The analysis of various dividend-related ratios indicates that the dividend payment patterns of the sample companies are irregular and exhibit a skewed distribution, suggesting the absence of a consistent dividend policy. Furthermore, the correlation matrix reveals a very weak positive relationship between the Dividend Payout Ratio (DPR) and the Price-to-Earnings (P/E) Ratio, which is statistically significant at the 5 percent level. Similarly, Earnings per Share (EPS) demonstrates a weak but positive association with both Return on Assets (ROA) and Return on Equity (ROE), with these relationships being significant at the 1 percent level. In addition, a strong positive correlation is observed between ROE and ROA, which is also statistically significant at the 1 percent level, indicating a close relationship between these two profitability measures. In this study two regression models were also used (i) *Model I: ROA c DPR PER EPS* and (ii) *Model II: ROE c DPR PER EPS*. The random effect regression model is adequate because both models' results were significant. It is possible to draw the conclusion that the dividend policy of businesses in the information technology sector is significantly influenced by the firm's performance.

7. IMPLICATIONS OF THE STUDY:

The Information Technology (IT) sector plays a pivotal role in the Indian economy, serving as one of the primary contributors to the country's service sector and Gross Domestic Product (GDP). Dividend policy and dividend distribution practices have long been subjects of considerable interest and debate in the field of finance. The findings of this study may provide valuable insights for investors, managers, and other stakeholders involved in investment and profit-planning decisions. Furthermore, the study contributes to a better understanding of dividend policy, which remains one of the most complex and extensively discussed issues in corporate finance. The significance of this research is further enhanced by its attempt to develop and evaluate appropriate dividend policy frameworks that can support effective financial decision-making and improve corporate performance.

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