REVIEWED JOURNAL INTERNATIONAL of BUSINESS MANAGEMENT
ISSN 2663-127X

Vol. 2, Iss. 1 (2021), pp 80 – 85, December 29, 2021. www.reviewedjournals.com, ©Reviewed Journals

RELATIONSHIP BETWEEN SALES GROWTH AND DIVIDEND PAYOUT. A STUDY OF LISTED COMPANIES IN KENYA

Teresiah Muthoni Chumari

Department of Finance & Accounting, School of Business, University of Nairobi [UoN], Kenya

Accepted: December 2, 2021

ABSTRACT

This study analyzed the relationship that exists between dividend payout and sales growth. The study adopted a descriptive research design. Thirty financial statements of listed companies was analyzed. The research also advanced the work of previous scholars and academicians. Based on this research the results showed that there was a negative relationship between dividend payout and sales growth. This study recommended that firm managers should plan on the proportion of profits that should be retained versus the portion that will be distributed as dividends to stockholders. Managers are also rated on financial performance hence the findings of this study would be of great benefit to them and would also act as a guide to setting reliable corporate dividend policies.

Key Words: *Sales Growth, Divided Payout*

INTRODUCTION

Brealy, Myers & Marcus (2007), isolated payout policy from other problems of financial management by asking a question on the effect of a change in payout policy given the firm's capital budgeting and borrowing decisions. If a firm proposes to increase its dividend, the cash to finance that dividend has to come from somewhere. Fixing the firm's investment outlays and borrowing leaves only one possible source which is to issue stock. If a firm decides to reduce its dividend it will have extra cash. If investment outlays and borrowing are fixed repurchasing stock is the only one possible way that this cash can be used. The payout policy therefore involves a tradeoff between higher or lower cash dividends and the issue and repurchase of stock. There exist three opposing point views with payout policy. On one side there is a group that believes high dividends increase value. On the other side there is a

CITATION: Chumari, T. M. (2021). The relationship between dividend payout and sales growth: A study of listed companies in Kenya. *Reviewed Journal International of Business Management*, 3 (1), 80 – 85.

group that believes high dividends bring high taxes and therefore reduce firm value and in the third party believes payout policy makes no difference.

According to Amidu & Abor (2006) a negative relationship is expected to exist between sales growth, market-to-book value and dividend payout. Growth in sales and market-to-book values represent firm's future prospects and investment opportunities. Growing firms require more funds in order to finance their growth and therefore would typically retain greater proportion of their earnings by paying low dividend. Also, firms with higher market-to-book value tend to have good investment opportunities and thus would retain more funds and record lower dividend payout ratios.

Research Problem

A negative association is expected between dividends pay out and sales growth. This relationship between dividend payout and its determinants has been studied empirically in Kenya.

Adedeji (1998) tested whether the pecking order hypothesis explained the dividend payout ratios of firms in the United Kingdom (UK). The evidence indicated that financial leverage had a positive interaction with dividend payout ratio but no significant interaction with investment. He also observed that irrecoverable advance tax had a positive, albeit weak influence on dividend payout ratio and overseas profit had a negative influence on the ratio.

Nissim & Ziv (2001) investigated the relationship between dividend changes and future profitability, measured in terms of either future earnings or future abnormal earnings. They found out that dividend changes provided information about the level of profitability in subsequent years, incremental to market and accounting data. They also found out that dividend changes were positively related to earnings changes in each of the two years after the dividend change.

Arnott & Asness (2003) investigated the relationship between payout and future earnings growth in the United States (US) market. They found out that the historical evidence strongly suggested that expected future earnings growth was fastest when current payout ratios were high and slowest when payout ratios were low. Farsio, Geary & Moser (2004) examined the relation between dividends and earnings. Their study revealed that there was no significant relation between dividend policy and earnings in long run. They recommended that different possibilities of relationship between future earnings and dividend should be analyzed. The theoretically expected relationship between dividend payout and sales growth were very clear but the empirical findings showed mixed results. This study tested the relationship between dividend payout and sales growth of the thirty firms listed on the Nairobi Securities Exchange as at 31st December 2013.

Research Objective

The objective of this study was to test the relationship between dividend payout and sales growth of stocks listed in the Nairobi Securities Exchange.

LITERATURE REVIEW

Clientele Effect Theory

This theory developed by MM (1961) argues that a firm attracts shareholders whose preferences in respect to payment of dividends correspond to the pattern of payment adopted by the firm itself. Some shareholders desire stable dividends as a source of income while others may prefer a capital gain. For example retirees and the poor generally prefer cash income, so they may want the firm to pay out higher percentage of its earnings. Such investors are often in low or zero brackets, so taxes are of no concern.

On the other hand, investors in their peak earning years might prefer re-investment, because they have less need for current investment income and would simply reinvest dividends received after paying income taxes on their dividends. Investors who want current investment income should own shares in high dividend payout firms, while investors with no need for current investment income should own shares in low dividend payout firms. Therefore dividend policy adopted by the firm in the past should be maintained into the future as it serves a preferred clientele.

Empirical Review

Amidu & Abor (2006) in examined the determinants of dividend payout ratios of listed firms in Ghana for a six year period 1998-2003. A sample of 20 firms out of 29 firms was selected for analysis. They used panel data methodology that is panel regression. Dividend payout ratio was the dependent variable and the independent variables were profitability, cash, institutional holdings of equity stock, risk (variability in profit), tax, growth in sales and market-to-book value. They found statistically significant and positive relationship between dividend payout ratio and profitability, cash flow and tax. The results also showed a negative association between dividend payout and risk, institutional holding, growth and market-to-book value.

Mbuki (2010) studied factors that determine dividend payout ratio among Savings and Credit Cooperative Societies (SACCO) in Kenya. The data was collected in September 2010. Out of 5,000 registered SACCO's in Kenya, a sample of 25 SACCO's was selected and the mode of selection was based on the fact that the 25 SACCO's have their headquarters in Nairobi. The results were analyzed using regression method. Dividend payout ratio was the dependent variable while the independent variables included profitability, sales growth, cash flow, size and risk. The study established that SACCO's profitability, growth opportunity, cash flow and size variables positively influenced dividend payout ratio, while risk variable negatively influenced dividend payout ratio.

Kibet (2012) conducted a study on the effect of liquidity on dividend payout by companies listed at the Nairobi Securities Exchange for a five year period (2007-2011). He sampled 34 companies out of the 57 listed. Firms under finance and investment sector were not considered because they did not have a uniform debt and assets structure like other firms quoted in other sectors. He used multivariate regression analysis where dividend payout was the dependent variable while liquidity, leverage, profitability, cash flow, corporate tax, sales growth and earnings per share were the independent variables. He found a positive relationship between dividend payout and leverage, profitability, corporate tax, sales growth, industry and earnings per share. He also found a negative association between dividends pay out and cash flow.

METHODOLOGY

The proposed study used descriptive research design. Cooper & Schindler (2011) defines descriptive research design as a research design concerned with finding out who, what, where, or how of the research. The population of the proposed study consisted of the thirty stocks listed in the NSE as at 31st December 2013. Financial statements were analyzed for a period of five years that is from year 2008 to year 2012 for thirty listed companies (Excluding banks and insurance companies). All variables were calculated as follows;

Sales Growth (GROW**)** = Growth in sales for firm I.

$$\textbf{GROW} = \frac{(\text{Current sales} - \text{Previous sales})}{\text{Previous sales}}$$

RESULTS

Linear regression was done to try and bring out clearly the relationship between dividend payout and sales growth, that is, whether it has a positive or negative relationship to the dividend payout.

Standard co-efficient for the financial performance variable for the 5 years was above 0.10 and hence this showed that it was significantly related either positively or negatively to the dependent variable, that is, dividend payout.

Correlation co-efficient which showed the relationship between the study variable was conducted. From the findings there was a strong relationship between the study variables.

From the regression output, it was revealed that sales growth to a standardized co-efficient of a constant zero, the payout ratio of the firms listed at NSE would stand at 26. 1643, a unit increase in growth would lead to a decreased in dividend payout by a factor of 1.9385. This showed that dividend payout had a negative relationship on sales growth. The study found that there was a negative relationship between dividend payout and sales growth.

CONCLUSION AND RECOMMENDATIONS

The study revealed that sales growth is statistically significant in influencing the dividend payout ratio negatively. The study found that there was a negative relationship between dividend payout and sales growth. This can be explained by the fact that growth in sales represents firm's future prospects and investment opportunities. Growing firms require more funds in order to finance their growth and therefore would typically retain greater proportion of their earnings by paying low dividend. Managers should take keen interest on sales growth since it has a significant effect/impact on dividend payout. This study can be repeated with a wider population of study by including the Banks and Insurance Companies across all countries in East Africa, African and European Continents. This paper further recommended that this study can be done on different economies to make the findings relevant to all various countries with different economic levels.

Suggestions for Further Study

A similar study to be done in other firms not listed in NSE. The same study can be done on Banking and Insurance Companies. It can also be done in other Companies with different economies level. The study can be done in other countries.

REFERENCES

Adedeji, A. (1998). Does the pecking order hypothesis explain the dividend payout ratios of firms in the UK? *Journal of Business Finance & Accounting*, *25*(9-10), 1127-1155.

Amidu, M., &Abor, J. (2006).Determinants of dividend payout ratios in Ghana. *Journal of Risk Finance, The*, *7*(2), 136-145.

Arnott, R. D., &Asness, C. S. (2003). Surprise! Higher dividends= higher earnings growth. *Financial Analysts Journal*, 70-87.

Bashir, Z, Abbas, A, Manzoor, S &Akram, M.N. (2013). Empirical investigation of factors affecting firm's performance: a study based on food sector of Pakistan. *International SAMANM Journal of Finance and Accounting*,1(2).

Bitok, K., Tenai, J., Cheruiyot, T., Maru, L. &Kipsat, M. (2010). The level of corporate dividend payout to stockholders: Does optimal dividend policy exist for firms quoted at the Nairobi Securities Exchange?*International Business & Economic Research Journal*, 9(3).

Black, F. (1976). The dividend Puzzle. *Journal of Portfolio Management,* 5(8)

Brealy, R.A, Myers, S.C & Marcus, A, J. (2007). Fundamentals of Corporate Finance. Boston: McGraw Hill Irwin

Dilawer, T. (2012). Earning Management and Dividend Policy: Evidence from Pakistani Textile Industry. *International Journal of Academic Research in Business & Social Sciences*, *2*(10).

Farsio, F, Geary, A & Moser, J. (2004). The relationship between dividends and earnings. *Journal for economic Educators*, 4(4), 1-5

Grossman, S. J., & Hart, O. D. (1982). Corporate financial structure and managerial incentives. In *The economics of information and uncertainty* (pp. 107-140). University of Chicago Press.

Hanif, H. (2014). The Dynamic Relationship among Dividend, Earning and Investment: Empirical Analysis of Karachi Stock Exchange. *International Journal of Management and Business Research, 4*(1), 55-63.

Howatt, B., Zuber, R. A., Gandar, J. M., & Lamb, R. P. (2009). Dividends, earnings volatility and information. *Applied Financial Economics*, *19*(7), 551-562.

Jensen, M. &Meckling, W. (1976).Theory of the Firm: Managerial Behavior, Agency Costs, and Capital Structure. *Journal of Financial Economics* 76, 323-339.

Jensen, M. C. (1986). Agency costs of free cash flow, corporate finance, and takeovers. *The American economic review*, 323-329.

Kibet, P. K. (2012). The effect of liquidity on dividend payout by companies listed at the Nairobi Securities Exchange. Unpublished MBA project, University of Nairobi.

Krishnan & Moyer (1997). Performance, Capital Structure and Home Country: An analysis of Asian Countries. *Global Finance Journal*, 8(1), 129-143.

Mbuki, C. (2010). Factors that determine dividend payout ratio among Sacco's in Kenya. Unpublished MBA project, University of Nairobi.

Memon, F., Bhutto, N.& Abbas, G. (2012). Capital Structure and firm's performance: A case of sector of Pakistan. *Asian Journal of Business and Management Sciences*, 1, (9), 9-15.

Nissim, D., &Ziv, A. (2001). Dividend changes and future profitability. *The Journal of Finance*, *56*(6), 2111-2133.

Njuguna, I.M (2006). Determinants of dividend payout: Case of listed companies in Kenya. Unpublished MBA project, University of Nairobi.

Nosa&Ose, (2010). Capital Structure and Corporate Performance in Nigeria: An empirical investigation. *Journal of Management Sciences*, 1(1), 43-52.

Omran, M., &Pointon, J. (2004). Dividend policy, trading characteristics and share prices: empirical evidence from Egyptian firms. *International Journal of Theoretical and Applied Finance*, *7*(02), 121-133.

OnaolapoandKajola (2010). Capital structure and Firm's Performance: Evidence from Nigeria. *European Journal of Economics, Finance and Administration Sciences*, 25, 70-82.

Welch, I. (2009). Corporate Finance an Introduction. New York: Pearson Education International

Williams, J. (1987). Perquisites, risk, and capital structure. *Journal of Finance*, 42, 29–49.

Parsian, H., Koloukhi, A. S. &Abdolnejad, S. (2013). The relationship between dividend payouts ratio and future earnings growth, a case of listed company in Iran market. *Interdisciplinary Journal of Contemporary Research in Business,* 5 (4).

Ross, A. S, Westerfield, R.W & Jaffe, J. (1999) Corporate Finance. Boston: Irwin McGraw-Hill

Yegon, C., Cheruiyot, J., Sang, J., Cheruiyot, P.K., Kirui, J. & Rotich, J. (2014). Effects of dividend policy on Firms's Financial Performance: Econometric Analysis of listed Manufacturing firms in Kenya. *Research Journal of Finance & Accounting*, 5(12).

Zeitun, R., and Tian, G.G., (2007). Capital Structure and Corporate performance: Evidence from Jordan. *Australasian Accounting, Business and Finance Journal*, 1(4).