Modeling of Dividend Policy: A Comparison between Malaysia Financial and Non-Financial Industries

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ABSTRACT

Dividend policy is a decision of management about the portion of income that is given to shareholders in the form of a dividend. In order to make a decision on dividend policy, this study aims to investigate the factors that could determine dividend policy on financial and non-financial industries in Malaysia. The internal factors that had been taken for this study are profitability, size, liquidity, leverage and growth opportunity of the firms. The model consists of the dependent variable which is Dividend per Share (DPS) as a proxy for dividend policy for both financial and non-financial industries. All required data were retrieved from the year 2005 until the year 2014 on an annual basis. The selections of companies are based on the most profitability and high dividend per share within these industries. The method used to analyze the panel data for this study is multiple linear regressions. The findings showed that profitability, firm size and growth has significantly determined dividend policy for both financial and nonfinancial industries. However, it seems dividend policies for the financial industry are determined by profitability, firm size and liquidity. While, only profitability and growth were determined dividend policy for non-financial industry.
KEYWORDS: Dividend Policy, Profitability, Firm Size, Liquidity, Leverage, Growth Opportunity.

INTRODUCTION

Dividend policy is the policy that company used to decide how much it will pay out to shareholders in dividends [5]. Basically, the decision whether to issue dividends and its amount are determined mainly on the consideration of the company's appropriate profit. Moreover, when cash surplus exists and is not needed by the firm then management is expected to pay out some or all of those surplus earnings in the form of cash dividends or to repurchase the company's stock through a share buyback program. However, the factors that influence the dividend policy may differ for different industries. Study on two different industries will confirm whether different industries will consider different factors in determining its dividend policy. In Malaysia, two industries that contributed towards Malaysia economy consist of financial and non-financial industries. Financial industries focus on dealing with financial transactions such as investments, loans and deposits. In specific, financial industries can be divided into banking and finance company. The non-financial industries do not deal with financial or investment-related goods or services. It consists of a few sectors consist of consumer product, industry/production, construction, trading/services, technology, Association Connecting Electronics Industries (IPC), properties, plantation and real estate investment trust (REIT). Therefore, this study has been done in order to determine the relationship between internal factors and divided policy for different types of industries.

LITERATURE REVIEW

Dividend Policy
There is a large literature dealing with factors that influence the dividend policy. For example, in [11] did the first empirical studies of dividend policy and he performed a survey of personnel of large firms in the United States of America to understand how the corporate managers arrived at the dividend policy. According to [20], dividend payout as distributions of retained earnings for the investors "shareholders" based on their proportionate ownership. Dividends are usually paid in cash, but sometimes paid in stock or other means. Firms always look for an optimal dividend policy, among others to reach equilibrium among current dividend, future growth and maximize firm's stock price. In [15] discussed dividends were irrelevant and had no influence on a firm's share price. They believed in the world of an efficient market that dividend policy does not affect the shareholder wealth. However, in [6] discuss that a return in the form of dividends is a sure thing but a return in the form of capital gains is risky. Therefore, firms should set a large dividend payout ratio to maximize firm share price.

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Profitability

In [14] Stated that profitability and size are the most important considerations of dividend payout decision by UEA firms. In [10] also agreed that profitability shows stronger positive linear relationship with dividend yield and dividend payout ratio. In [16] also stated that profitability influence positively and business risk impacts negatively on dividend disbursement. In [17] strongly supporting for size, age and profitability of the firm seem to be a determinant factor of corporate dividend policy in Jordan. On the other hand, in [15] stated that profitability has been found significantly associated with a dividend payout ratio and Pakistan maturity of firms does not have any effect on dividend policy.

Firm Size

The previous study was done by [5], when the firm increases its size is earning and foreign ownership will also increase with that, so these firms pay a constant dividend to keep our investors satisfied according to their size and earning capacity. In [19] stated that among controlled variables, profitability, firm size and the ratio of retained earnings to book equity have positive effects on a firm's decision whether to pay dividends and how much to pay dividends. The firm size is positive and significant, supporting the idea that larger firms have easier access to fund and are able to distribute dividends to shareholders better than smaller firms. The larger firm chooses to pay a higher dividend [13]. However, there are a few previous studies inversely found the result of firm size. In [7] found that size, leverage, agency cost, growth and risk do not have any significant impact on the dividend behavior of Pakistani banks.

Liquidity

According to [4], liquidity is the extent at which a firm can pay short-term liabilities based on its liquid assets. In [8] found that the most liquid firms in Japan have higher dividend payouts. Besides that, it had been recorded a few numbers of studies have suggested that firms with a greater "cash flow" need to pay more dividends to reduce the agency costs of the free cash flow [9]. Based on the findings of the studies, it can be concluded that there is a positive relationship between the cash flow and the dividend payout ratio. According to [3], a firm with high external financing would require the availability of cash flows, i.e. strong liquidity position to meet its financial obligations. Therefore, in order to increase liquidity, the firm shall lower its dividend payout. There are previous researches defined that liquidity and dividend policy have an inverse relationship and not related. It can be proved by taking research from [10], there is no relationship between liquidity and cash dividend. Meanwhile, in [2] stated that paying lower or a higher dividend does not depend on a good or bad liquidity position. Other than that, based on research [18] found that firms with high level of profitability and liquidity prefer retaining their cash for debt settlement and/or investment rather than paying out dividends.

Leverage

The result of the study conducted by [12] shows that size, leverage and industry is significant with dividend policy. In [1] stated that financial leverage was found to have a negative impact on dividend payout, which indicating fewer dividend payments by high-debt firms. According to [8], there is no relation between debt ratios and dividend policy. In the research done by [2], the results indicate that there exists an inverse relationship between dividend rate and leverage. In [1] stated that debt ratio (leverage) and dividend yield are found to be the most influential variables affecting the dividend payout policy of the corporate sector of Pakistan.

METHODOLOGY

This correlational type of study assessed the relationship between profitability, firm size, liquidity, leverage and growth towards dividend policy for financial and non-financial industries within Malaysia. This study involved the use of pooled regressions with panel data. Panel data in this study refer to the data set consist of several number of companies from financial and non-financial industries for period started in 2005 until 2014. The panel data collected based on secondary sources were analyzed by using the EVIEWS version 8. The analysis started with the descriptive analysis in related to frequencies, the mean and the standard deviation which provide descriptive information about a set of data. It followed by correlation analysis to identify the correlation that exists between the independent variables. In order to test hypotheses developed, this study used the method of pooled Multiple Linear Regressions and finding were remarked.

Three hypotheses were developed for both models:

H1: There is a relationship between profitability towards financial or non-financial industries dividend policy.
H2: There is a relationship between firm size towards financial or non-financial industries dividend policy.
H3: There is a relationship between liquidity towards financial or non-financial industries dividend policy.
H4: There is a relationship between leverage towards financial or non-financial industries dividend policy.
H5: There is a relationship between growth towards financial or non-financial industries dividend policy.

FINDINGS AND DISCUSSION

The study intended to study the relationship between profitability, firm size, liquidity, leverage and growth towards dividend policy for financial and non-financial industries within Malaysia. Pearson Product-Moment Correlation Coefficient was used to assess the relationship among variables (independent and dependent variables). Table 1 shows the result from Pooled Regression Method on model 1 and model 2 that represent financial and non-financial industries.

Table 1: Pooled regression analysis

Variable	Comparison Study on Financial and Non-Financial Industries					
	Model 1: Financial Industry $Y_i = \alpha + \beta_1 X_{1i} + \beta_2 X_{2i} + \ldots + \varepsilon$			Model 2: Non-Financial Industry $Y_i = \alpha + \beta_1 X_{1i} + \beta_2 X_{2i} + \ldots + \varepsilon$		
	Financial Industry			Non-Financial Industry		
	Coefficient	t-Statistic	Prob.	Coefficient	t-Statistic	Prob.
Profitability	3.934463	4.188318	0.0001***	3.990464	13.03101	0.0000***
Firm Size	0.052251	3.173715	0.0027***	0.023125	0.715837	0.4761
Liquidity	-0.047035	-2.979289	0.0047***	0.000109	0.196484	0.8447
Leverage	-0.000353	-1.029205	0.3090	-0.000727	-0.970662	0.3345
Growth	0.035889	0.910618	0.3675	-0.083250	-1.764529	0.0813*
C	-0.347460	-2.161093	0.0362	-0.252745	-0.881335	0.3807
Overall Model Evaluation						
R-squared	0.374185			0.737430		
Adjusted R-squared	0.303070			0.721800		
F-statistic	5.261671			47.18282		
Prob (F-statistic)	0.000714			0.000000		
Durbin-Watson stat	1.804740			0.398381		

Notes: P-value in parentheses, ***Significant at the 1% level, **Significant at the 5% level, *Significant at the 10% level. Cross section time period is from 2005-2014 and including observations number of 50 for the financial industry and 90 for the non-financial industry.

It seems that for model 1, profitability, firm size and liquidity were significant at the 1% level of significant. Therefore, this study failed to reject alternate hypotheses developed for H1, H2 and H3. While, there is no significant relationship between leverage and growth towards the dividend policy of the financial industry. Hence, H4 and H5 are failed to accept by this study. In contrast, for model 2 findings showed that only probability and growth has significant relationship toward dividend policy of non-financial industry. Therefore, this study is failed to reject H1 at the 1% significant level and H4 at 10% significant level. Based on the findings, it can be concluded that both industries will have a decision of management about the portion of income that is given to shareholders in the form of a dividend by considering the amount of profitability income they have.

CONCLUSION AND RECOMMENDATIONS

There are many studies have been conducted on the determinant of dividend policy and have suggested different findings of the determinant of dividend policy. The aim of this study is to investigate the determinant of financial and non-financial industries dividend policy in Malaysia. The internal factors that had been taken for this study are profitability, firm size, liquidity, leverage and growth opportunity of the firms. The model consists of the dependent variable which is Dividend per Share (DPS) as a proxy for dividend policy for both financial and non-financial industries. All required data were retrieved from the year 2005 until the year 2014 on an annual basis. Based on the objective of this study, multiple linear regressions have been used with panel data. There are 140 numbers of observations. Finding showed that profitability, firm size and liquidity have a significant relationship to its dividend policy. While, only profitability and growth have a positive significant relationship towards dividend policy of non-financial industries. In conclusion, for both industries, profitable firms will distribute more in the form of a dividend to investors. Understanding the determinants of dividend policy has a significant implication for investors, shareholders and portfolio analysts. Based on this study finding, besides profitability, investors will also consider the firm size and firm liquidity level to buy shares of the firms from financial industries. The higher the profitability, size and liquidity level of the firm will promise investors to receive an appropriate dividend payment. However, investors' intentions to buy shares of the firm from non-financial industries are reflected the firm's profitability and growth. The most profitable and higher growth of the firm will result in higher dividend payment. For further study on dividend policy, external factors such as the macroeconomic factors should be including to see whether these factors also affect dividend policy for both industries.

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