PalArch's Journal of Archaeology of Egypt / Egyptology

The Effect Of Dividend Payout On Profitability: An Empirical Study On Information Technology Industry In India

***Dr.T.Narayana Reddy* [1] *and Mr.Kathari Santosh* [2]**

[1]Associate Professor, Department of Management Studies and Additional Controller of Examinations, JNTUA College of Engineering, JNTU Anantapur, Ananthapuramu, India, e-mail: tnreddyjntua@gmail.com

[2]Assistant Professor, Department of MBA, CMR Institute of Technology, Bengaluru, Karnataka, India, e-mail: katarisantoshmba@gmail.com.

Dr.T.Narayana Reddy [1] and Mr.Kathari Santosh [2], The Effect Of Dividend Payout On Profitability: An Empirical Study On Information Technology Industry In India, - Palarch's Journal Of Archaeology Of Egypt/Egyptology 18(4). ISSN 1567-214x, Key words: IT Companies, Dividend payout, Correlation, Profitability and Regression.

Abstract

The aim of this study to determine relationship between dividend payout and firm profitability among top information technology companies in India. The present study carried on the basis of secondary data. For analyzing data correlation and multiple regression analysis were applied. Based on the result of analysis TCS has significant relationship between profitability and dividend payout and remaining companies are not significant. But based on the correlation analysis, majority of the companies have strong positive correlation between dividend payout and profitability. Hence the study concludes that dividend payout and firm profitability is relevant with dividend policy and also it will improve shareholders wealth.

Key words: IT Companies, Dividend payout, Correlation, Profitability and Regression.

1. Introduction:

According to the Institute of Chartered Accountants of India, dividend is "a distribution to shareholder out of profits or reserves available for this purpose".

Dividend has an impact on market price of company's share and its profitability which is a debatable statement. Some financial analysts believe that dividends affect the market price of shares and few are not accepting this statement. But it has been proved that dividends have an important effect on share price and profitability of the firm. There are five important reasons why dividend matters for investors, include the fact they extensively raise stock investing profits, offer an extra metric of fundamental analysis, reduce overall portfolio risk, offers tax advantages and help to maintain purchasing power of capital.

Dividend is explained as the portion of profit which is allocated to the shareholders of the company. It may be defined as the return that a shareholder gets from the company, out of its profits, on his shareholdings.

Expansion and Growth in Profits

Investors believe one of the primary benefits of investing in dividend paying companies is that dividend tend to steadily grow over a period of time. Highly established companies pay dividend typically to increase dividend payouts from year to year. There is a number of "dividend aristocrats," or companies that have continuously increased their dividend payouts for more than 25 years consecutively. The dividend average Compound Annual Growth Rate (CAGR) for Standard &Poor (S&P) Companies that offers dividend has been 3.2%.

There is always up and down of stock, but there is no assurance to increase in its price. If you want to invest your money into dividend paying companies, there is no guarantee to get more profits. But these companies give better return on investment. Even most of the dividend paying companies continuously declares the dividends to the shareholders over time.

Volatility of stocks and risk reduction:

Dividend is major factor to reduce overall portfolio risk and volatility. In terms of reducing risk, payment of dividend can moderate any losses that occur from a decline in stock price. But the risk reduction benefit of dividends goes beyond that basic fact. Most of the studies proved that, dividend paying companies performs extensively and non-dividend paying companies perform less during bear market periods.

Valuation of Equity

Dividends are helpful for equity valuation. One of the most useful equity valuation measures than others, such as Price to Earnings Ratio (or) P/E Ratio.

Tax efficiency

Dividend offers tax advantages. These are extremely tax efficient for obtaining income; some qualified dividends are taxed at lower rates. As Per Income Tax Regulations (IRS) of 2011, whose individual income tax rate is 25 per cent or higher, qualified dividends are taxed at 15 per cent rate. The remaining portion below 25 per cent income tax, qualified dividends are tax-free.

2. Review of Literature

Sartono (2001) states that, if the companies earn more profits usually they were pay dividend to the shareholders or transferred to retained earnings. The companies have more profitability, there is more scope to expand or diverse their business using retained earnings. **Sudasri (2002)** found that profitability affects the dividend policy of the firm. Dividend is distributed to the shareholders from profits after meet with their obligations like taxes and interest payment. **Samy Ben Naceur and Mohamed Goaied (2002)** indicate that the probability of creating future values is positively and significantly correlated with profitability factor. In addition, the results also suggest that the value creation is affected by industry patterns. **Ismiyanti & Hanafi (2003)** profitability is measured by return on assets. The Company's ability to produce profits at the rate of sales, property and certain capital is called profitability. They found that, profitability analysis is the major concern of long-term investors and shareholders will see the profits in terms of dividend also. **Gitman (2003)** states that, the relationship between revenues and costs are generated using profitability demonstrates the ability of capital invested in total assets to generate profits and also when there is greater level of profitability, more chances to declare the dividend. It means company's earning profits have impact on the dividend policy. **Amidu (2007)** found that statistically significant and negative relation between profitability and dividend payout and also found a negative association between firm's profitability measured by return on assets and return on equity with dividend payout.

Okpara, & Chigozie, G (2010) have found the negative but significant relationship between the dividend payout ratio and current profit. Furthermore they also used Earning per share ratio as an indicator for organizations current and future earnings structure. **Kohli et al. (2011)** in their study stated there exist a direct and positive relationship between dividend policy and the company's profitability. Profitability ratio is used to measure the earning capacity of the assets of an organization. It is very important for the shareholders to put their eyes on the company's financial conditions. The companies were able to pay good amount of dividend if they could earn more from the goods and services produced. Unsteady and unreliable earnings may be negatively affected on the dividend payout. **Timothy Mahalang'ang'a Murekefu and Ochuodho Peter Ouma. (2012)** found that dividend payout was a major factor affecting firm performance. Their relationship was also strong and positive. **Priya, K and Nimalathasan, B. (2013)** states that dividend policy ratios have a great impact on all firm performance ratios except return on investment (ROI) and return on equity (ROE). **Raluca Georgiana Moscu. (2014)** found that only variable influenced by the dividend per share, dividend in the previous year is the profit per share. **AR. Fathima Thafani and M.A. Mohamed Abdullah. (2014)** found that there was a significant relationship between dividend payout and corporate profitability in terms of return on assets, return on equity and earnings per share. **Dada F.B et al. (2015)** attempted to study the determinants of the dividend policy and its profitability of Nigerian banking sector. They concluded that leverage, corporate governance, profitability and last year dividend had positive impact and firm's liquidity had negative impact. **Bogna Kaźmierska-Jóźwiak. (2015)** found that statistically significant and negative relationship between dividend payout ratio (DPO) and two analyzed factors: profitability (ROE) and leverage (LEV) and also states that dividend payout ratio is a negative function of profitability and leverage. **Mensah Mawutor et al. (2015)** found that profitability and dividend policy are significantly related. Thus, when the banks make profits they tend to pay out dividends. However, the study also shows through a regression model that banks listed on the Ghana stock exchange employ a dividend policy that is not solely influenced by profitability. **Ishtiaq Ahmad and Muhammad Fahid Muqaddas. (2016)** found that statistically significant association of safety, risk and profitability with dividend payout ratio. **Khadija Farrukh et. al. (2017)** found that dividend policy has positively significant impact on shareholders' wealth and firm performance. It supported dividend relevance theory, signaling effect theory, bird in hand theory and clientele-effect theory. **Muhammad Tamrin et.al. (2017)** proved that profitability has a negative and significant effect on dividend policy. Profitability has a negative and significant effect on firm value. Dividend policy has positive and insignificant effect on firm value. **Hirindu Kawshala and Kushani Panditharathna (2017)** concluded that there is a positive significant relationship between dividend policy and the profitability in Beverage, Food & Tobacco (BFT) industry in Sri Lanka. **Manjunatha K and Akash S.B (2018)** found that relationship between Return on Assets and Dividend Payout Ratio is negative but statistically significant. **Jahangir Chauhan et.al (2019)** found that there is a strong relation between Return on Equity and Return on Assets. Hausman Test reveals that random affect model is appropriate thereby indicating that performance of selected companies have significant impact on dividend policy of selected companies. **Niway Ayalew Adimasu. (2019)** indicated that there is positive and significant relationship between profitability and dividend pay-out policy decision of Ethiopian private insurance companies.

Research Problem

From the literature review, In India very few studies have been done to establish the relationship between firms dividend payout and profitability. This study comes into fill the gap by establishing whether there is a relationship between profitability of the firm and dividend payout among the top five information technology companies in India for the year 2015 – 2020.

Research Questions:

The following questions have been addressed in order to gain an insight and understand the dividend payout and profitability in top IT firms in India.

- Is there any relationship between the firm profitability and dividend payout of top IT companies in India?
- What is the extent of the association between firm profitability and dividend payout of top IT companies in India?

3. Objectives of the present study:

- To examine the relationship between firm profitability and dividend payout among the top five IT companies in India.

Hypothesis of the study:

H_0: There is no significant relationship between the dividend payout and net profit.
H_{01}: There is no significant relationship between TCS dividend payout and net profit.
H_{02}: There is no significant relationship between Infosys dividend payout and net profit.
H_{03}: There is no significant relationship between HCL Tech dividend payout and net profit.
H_{04}: There is no significant relationship between Wipro dividend payout and net profit.
H_{05}: There is no significant relationship between Tech Mahindra dividend payout and net profit.

4. Research Methodology:

The present study used secondary data for the analysis. The data utilized in this study is extracted from the comprehensive income statements and financial position of the sample top five IT companies namely TCS, Infosys, HCL Tech, WIPRO and Tech Mahindra in India from 2016-2020.

The present study, for analyzing data we have employed correlation analysis and linear regression using SPSS 20.0 Version. The following are the variables considered for regression analysis.

Dependent Variable: Net Profit (Firms Profitability)
Independent Variable: Dividend Payout (Equity Share Dividend)

5. Data Analysis

Table: 1
Correlation Analysis between Net Profit and Dividend Payout

Company Name	Correlation Value (r)	Interpretation
TCS	0.702	High Positive
Infosys	0.367	Low Positive
HCL Tech	-0.641	High Negative
WIPRO	0.133	Low Positive
Tech Mahindra	0.698	High Positive

Table-1 presents the correlation analysis between profitability and dividend payout. It can be observed that, two companies namely TCS and Tech Mahindra are high positive correlation between profitability and dividend payout and Wipro and Infosys are low positive correlation. HCL Tech has high negative correlation between profitability and dividend payout.

Table - 2: Results of Multiple Regression Analysis (TCS)

Model Summary

Model	R	R Square	Adjusted R Square	F Change	Sig. F Change	Durbin-Watson
1	0.848	0.798	0.724	16.28	.012	1.525

Source: Author Own Calculation through SPSS

Table - 3: Regression Coefficients

Variable	Un-standardized Coefficients B	Standardized Coefficients Beta	t -value	Sig.	H_0 : Rejected/ Accepted	VIF
(Constant)	250.468		0.760	0.352		
Dividend Payout	2.122	.848	4.128	0.010	Rejected	1.00

Dependent Variable: Net Profit

Table - 2 indicates the model summary of multiple regression analysis which is carried out through SPSS. The result of the model shows that the value of *R* is 0.848, which indicates a high correlation between dependent (Net Profit) and independent variable (Dividend Payout). The value of *R* square is 0.798. The p value of the model is 0.012 which is less than 0.05 indicating that the regression model is statistically significant and a fit model. The value of Durbin-Watson statistic is 1.525 which is free from autocorrelation problem.

Table – 3 illustrates the results of regression analysis for Net Profit and Dividend Payout. Results of multiple regression reveals that the p value of Dividend Payout is 0.010, which is less than .05 at 5 % level of significance. This indicates that there is a statistically significant relationship between net profit and dividend payout.

The following regression equation was obtained:

$Y = 250.46 + 2.122\ X_1 + e$

Table: 4

Regression Analysis between Profitability and Dividend Payout (Five Companies)

Company Name	P Value	H_0 (Accepted/Rejected)
TCS	0.014	Rejected (H_{01})
Infosys	0.543	Accepted (H_{02})
HCL Tech	0.243	Accepted (H_{03})
WIPRO	0.831	Accepted (H_{04})
Tech Mahindra	0.393	Accepted (H_{05})

Summary, Conclusion and Recommendations

Based on the findings, there is significant relationship between profitability and dividend payout. It means, an increase in the financial wellbeing of a firm tends to positively effect on the dividend payout level of firms. From the above analysis, only TCS has significant relationship between dependent and independent variables and other companies are not significant. But, in generally some companies are earning more profits and they are not declaring dividend due to expansion or diversification purpose. An important limitation of this paper is the period for which the data were sampled. To address this limitation, future research can increase sample size and including other sectors and as well as include other factors related to both variables.

References:

1. Sartono, A. (2001). Financial management theory and application. Yogyakarta: BPFE
2. Sudarsi, Sri. (2002). Analysis of Factors Influencing the Dividend Payout Ratio in the Banking Industry are Listed on the Jakarta Stock Exchange. 9(1): 76-88.
3. Naceur, S. B., and Goaied, M. (2002). The relationship between dividend policy, financial structure, profitability and firm value. Applied Financial Economics, 12(12): 843–849.
4. Ismiyanti, F and Hanafi MM (2003). Managerial Ownership, Institutional Ownership, Risk, Debt Policy and Dividend Policy: Analysis of Simultaneous Equations. Accounting National Symposium, 6: 260-277.
5. Gitman Lawrence J. (2003). Principles of Managerial Finance. (10^{th} edition) Pearson International.
6. Amidu, M (2007). How does Dividend Policy affect Performance of the firm on Ghana Stock Exchange? Investment Management and Financial Innovations, 4: 103-12.
7. Okpara, and Chigozie, G. (2010). A Diagnosis of the Determinant of Dividend Pay-Out Policy in Nigeria: A Factor Analytical Approach. American Journal of Scientific Research, 8: 57-67.
8. Kohli H., Sharma A and Sood, A (2011). Asia 2050: Realizing the Asian Century. Emerging Markets Forum.
9. Murekefu, Timothy Mahalang'ang'a and Peter Ouma, Ochuodho. (2012). The Relationship between Dividend Payout and Firm Performance: A Study of Listed Companies in Kenya. European Scientific Journal, 8(9): 199-215.
10. Priya, K and Nimalathasan, B. (2013). Dividend Policy Ratios and Firm Performance: a case study of Selected Hotels & Restaurants in Sri Lanka. Global Journal of Commerce & Management Perspective, 2(6): 16-22.
11. Georgiana Moscu, Raluca. (2014). Empirical Evidences Regarding Correlation between Dividend Policy and the Performance of Companies Listed on the Bucharest Stock Exchange. International Journal of Academic Research in Business and Social Sciences, 4(12): 445-450.
12. Thafani, AR. Fathima and Abdullah, M.A. Mohamed. (2014). Impact of Dividend Payout on Corporate Profitability: Evident from Colombo Stock Exchange. Advances in Economics and Business Management (AEBM), 1(1): 27 – 33.
13. Dada F.B., Malomo E. and Ojediran S. (2015). Critical evaluation of the determinants of dividend policy of banking sector in Nigeria. International Journal of Economics, Commerce and Management, 3(2): 1-11.
14. Kaźmierska-Jóźwiak, Bogna. (2015). Determinants of Dividend Policy: Evidence from Polish Listed Companies. Procedia Economics and Finance, 23: 473 – 477.
15. Mensah Mawutor et al., (2015). Analysis of the Relationship between Profitability and Dividend Policy of Banks on the Ghana Stock Exchange. International Journal of Empirical Finance. Research Academy of Social Sciences. 4(7): 407-417.

16. Ahmad, Ishtiaq and Fahid Muqaddas, Muhammad. (2016). Determinants of Dividend Payout Policy: An Empirical Study of Banking Sector of Pakistan. Applied Studies in Agribusiness and Commerce, 10(5): 101-106.
17. Khadija Farrukh et al. (2017). Impact of dividend policy on shareholders wealth and firm performance in Pakistan. Cogent Business & Management, 4: 1408208.
18. Tamrin, Muhammad, Rahman Mus, H., Sudirman and Aryati Arfah (2017). Effect of profitability and dividend policy on corporate governance and firm value: Evidence from the Indonesian manufacturing Sectors. IOSR Journal of Business and Management, 19(10): 66-740.
19. Kawshala, Hirindu and Panditharathna, Kushani (2017). The Effect of Dividend Policy on Corporate Profitability: An Empirical Study on Beverage, Food and Tobacco Industry in Sri Lanka. International Journal of Scientific and Research Publications, 7(8): 542-546.
20. Manjunatha, K and Akash, S.B (2018). Dividend Policy and Financial Performance of Indian Cement Companies –An Empirical Study. Journal of Management, 5(6): 157-165.
21. Jahangir Chauhan et al., (2019). Dividend Policy and Its Impact on Performance of Indian Information Technology Companies. International Journal of Finance and Accounting, 8(1): 36-42.
22. Adimasu. Niway Ayalew (2019). Dividend Policy and Firm's Profitability: Evidence from Ethiopian Private Insurance Companies. Journal of Finance and Accounting, 7(4): 116-121.

*****