THE EFFECTS OF EARNINGS ON DIVIDEND POLICY OF FIRMS LISTED AT THE DAR ES SALAAM STOCK EXCHANGE

BY:

ATHUMANI ISSA HEMED MCHOMVU

A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION, SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI

NOVEMBER, 2014

DECLARATION

This research project is my original work and has not been presented to any other institution or university.

Signed _____ Date _____

Athumani Issa Hemed Mchomvu

D61/79776/2012

This research project has been submitted for examination with our approval as the university supervisors.

Sign_____ Date _____

Mr. Cyrus Iraya
Department of Finance and Accounting
School of Business,
University of Nairobi

DEDICATION

I dedicate this project to my family for their encouragement throughout my course.

ACKNOWLEDGEMENTS

From the initial stages to the final draft of this project for the partial fulfillment of the Master of Business Administration degree, I owe an immense debt of gratitude to my supervisor Mr. Cyrus Iraya for his invaluable support towards this project. His constructive criticism, careful guidance and patience have been very instrumental to the completion of this project in time.

I would also like to thank Dar Es Salaam Stock Exchange for availing the data I so much needed to complete this project within the time allocated to me. Special thanks go to the proposal presentation panel and colleagues who were present during the presentation of this project proposal.

Finally, but most importantly, I sincerely thank our Almighty God for giving me the strength and providing means to undertake this study. To each of the above, I extend my deepest appreciation.

ABSTRACT

The main aim of this paper is to investigate on the effects of earnings on dividend policy of firms listed at the Dar Es Salaam Stock Exchange. Dividend policy has been analyzed for many decades which refers to the issue of how much of the total profit a firm should pay to its stockholders and how much to retain for investment so that the combined present and future benefits maximize the wealth of stockholders. This provided theoretical and empirical information from publications on earnings on dividend policy of firms. It summarizes the information from other researchers who have carried out their research in the same area of dividend policy and firm value. The study employed both quantitative method through analysis of the financial statements using various models and ratios to provide predominantly quantitative and qualitative data to the study. The target population as of October 2013 there are seventeen listed companies on Dar Es Salaam Stock Exchange. The study used secondary data which was obtained from the financial statements of the Listed Firms on Dar Es Salaam Stock Exchange from 2009-2013. The data analysis techniques included descriptive statistics like the mean, minimum, maximum and standard deviation. In addition, inferential statistics like correlation analysis and regression analysis. The dividend payout ratio is regressed against the five explanatory variables: profitability, risk, cash flow, growth and size. The findings in the study showed that correlation coefficient for all were positive valued indicating that the variables are positively related. From the regression model, a correlation coefficient value of 0.407 was established. This portends a very good linear relationship or dependence of dividend payout on earnings. From the study findings, it is evident that the most critical factors considered by a firm in coming up with a dividend policy are the expected cash flows, risk, profitability, growth and size of the firm. a correlation coefficient value of 0.407 was established. This portends a very good linear relationship or dependence of dividend payout on earnings. A coefficient of determination (R-square) value of 0.166 was established. Profitability, risk, cash flow, growth and size, according to the model summary from the data analysis, profitability, growth, cash flow, risk and size had a positive impact on the dividend policy. The research study concluded that earnings to some minimal extent, influenced the dividend policy of individual firms. Based on the findings of this research study, the following recommendations are made. Organizations should ensure that they have a good and robust dividend policy in place. It is also recommended that firms should maintain a clear and consistent dividend policy for the dividend policy to affect the value of the firm.

TABLE OF CONTENTS

DECLARATION ..... **ii**

DEDICATION ..... **ii**

ACKNOWLEDGEMENTS ..... **ii**

ABSTRACT ..... **v**

LIST OF ABBREVIATIONS ..... **ix**

CHAPTER ONE: INTRODUCTION **1**

1.1 Background of the Study 1

1.1.1 Dividend Policy 2

1.1.2 Earnings 3

1.1.3 Effects of Earnings on Dividend Policy of Firms 4

1.1.4 Dar Es Salaam Stock Exchange 5

1.2 Research Problem 6

1.3 Research Objective 9

1.4 Value of the Study 9

CHAPTER TWO: LITERATURE REVIEW **11**

2.1 Introduction 11

2.2 Theoretical Framework 11

2.2.1 The Bird-In-Hand Fallacy 11

2.2.2 Dividend Irrelevance Theory 12

2.2.3 Clientele Effect Theory 13

2.2.5 Agency Theory 14

2.3 Determinants of dividend policy 15

2.3.1 Profitability 16

2.3.2 Risk 16

2.3.3 Cash Flow 17

2.3.4 Growth 18

2.3.5 Size 19

2.4 Empirical literature 20

2.5 Summary of Literature Review 25

CHAPTER THREE: RESEARCH METHODOLOGY 26

3.1 Introduction 26

3.2 Research Design 26

3.3 Population 26

3.4 Data Collection Techniques 27

3.5 Data Analysis Techniques Model 27

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION 29

4.1 Introduction 29

4.2 Descriptive Statistics 29

4.4 Correlation analysis 30

4.4 Regression Analysis 31

4.4 Discussion of findings 33

CHAPTER FIVE: SUMMARY, CONCLUSIONS AND RECOMMENDATIONS 35

5.1 Introduction 35

5.2 Summary 35

5.3 Conclusion..... 36

5.4 Recommendations 37

5.5 Limitations of the Study 38

5.6 Recommendations for Further Studies 39

REFERENCES..... 41

Appendices I: Dar Es Salaam Stock Exchange Companies performance..... 48

LIST OF TABLES

Table 4.1: Average Performance 29

Table 4.2: correlation analysis 30

Table 4.3: Regression Model 31

Table 4.4: Analysis of Variance (ANOVA) 32

Table 4.5: Regression Coefficients Table 32

LIST OF ABBREVIATIONS

CMSA:	Capital Markets and Securities Authority
DSE:	Dar es Salaam Stock Exchange
EGM	Enterprise Growth Market
FMCG	Fast Moving Consumer Goods
FOSAs	Front Office Sacco Activity
FV:	Firm value
MM:	Miller and Modigliani
OTC:	Over-the-counter
SACCOs:	Savings and Credit Co-operative

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

This study attempts to determine the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange. Dividends according to (Horne, 2007) are payments to stockholders from a firms earnings, According to Knott (2004), they are payments made by a corporation to an equity investor. Moyer, et al. (2002) says that dividend is cash payments made to stockholders by the corporation. He further asserts that dividend can be paid either in cash or through bonus issue. A cash dividend involves payments of dividends in monetary form while bonus issue is the distribution of free ordinary share to the existing shareholders in proportion to their current ownership (Horne, 2007). The mode in which dividends are paid depends on the liquidity position of the company and the company's financial requirements. Bonus issue is used when the company is in liquidity problems (Pandey, 2005).

The amount of dividend paid to the investors depends on the company's dividend policy (Pandey, 2005). Dividend policy is the determination of which portion of cash earnings should be retained in the firm for reinvestment and which funds are paid out to investors from either current or accumulated retained earnings (Kania & Bacon, 2005). Gitman (2008) says that dividend policy involves the firm's decision to pay out earnings or retain them for reinvestment purposes. It is an integral part of a firm's financial decision as the payout ratio determines the amount to be retained in the firm as a source of internal financing.

1.1.1 Dividend Policy

The term 'dividend policy' refers to "the practice that management follows in making dividend payout decisions or, in other words, the size and pattern of cash distributions over time to shareholders (Lease et al., 2000). This issue of dividend policy is one that has engaged managers since the birth of the modern commercial corporation. Surprisingly then dividend policy remains one of the most contested issues in finance. The study of dividend policy has captured the attention of finance scholars since the middle of the last century. They have attempted to solve several issues pertaining to dividends and formulate theories and models to explain corporate dividend behaviour.

Dividend policy refers to the issue of how much of the total profit a firm should pay to its stockholders and how much to retain for investment so that the combined present and future benefits maximize the wealth of stockholders (Chawla & Srinivasan, 1987). The dividend policy, however, not only specifies the amount of dividend, but also form of dividend, payment procedure etc. Earnings is often able to predict approximately what its earnings will be. Such a firm is therefore more likely to pay out a higher percentage of its earnings than a firm with fluctuating earnings.

Dividend policy of a firm has implication/importance for investors, mangers and lenders and other stakeholders (more specifically the claimholders). For investors, dividends – whether declared today or accumulated and provided at a later date are not only a means of regular income, but also an important input in valuation of a firm. Similarly, managers' flexibility to invest in projects is also dependent on the amount of dividend

that they can offer to shareholders as more dividends may mean fewer funds available for investment. Lenders may also have interest in the amount of dividend a firm declares, as more the dividend paid less would be the amount available for servicing and redemption of their claims.

1.1.2 Earnings

The amount of profit that a company produces during a specific period, which is usually defined as a quarter (three calendar months) or a year. Earnings typically refer to after-tax net income. Ultimately, a business's earnings are the main determinant of its share price, because earnings and the circumstances relating to them can indicate whether the business will be profitable and successful in the long run (Teoh, Welch, Wong, 2008). Earnings are perhaps the single most studied number in a company's financial statements because they show a company's profitability. A business's quarterly and annual earnings are typically compared to analyst estimates and guidance provided by the business itself. In most situations, when earnings do not meet either of those estimates, a business's stock price will tend to drop. On the other hand, when actual earnings beat estimates by a significant amount, the share price will likely surge.

Earnings management is different from accounting frauds which violate Generally Accepted Accounting Principles, because the opportunities of earnings management are inherent in the current financial reporting system. (Kim, & Verrecchia, 2001) argue that the nature of accrual accounting gives managers considerable discretion in determining the earnings in any given period. According to Teoh, Welch, Wong, (2008) within the

boundary of GAAP, managers have several sources to manipulate earnings. They can choose an accounting method to advance or delay the recognition of revenues and expenses, use discretionary aspects of the application of the chosen accounting method, or adjust the timing of asset acquisitions and dispositions to alter reported earnings.

1.1.3 Effects of Earnings on Dividend Policy of Firms

According to Arif, et, al. (2011) in their study investigated the effect of earnings on dividend policy of companies listed in the Karachi Stock Exchange. Information and financial data of 86 companies during the period 2004-2009 form the statistical sample of this study. In this study, the discretionary accrual that is calculated by adjusted Jones model is used as an indicator for earnings management. The results indicate that there is no significant relationship between discretionary accruals and dividend policy of companies.

In addition, they found that smaller firms than larger firms pay more dividends. This study shows that managers are not involved in dividend policy and there may be some other motivations behind earnings management. MM theory implies that dividend payout will fluctuate as a by-product of the firm's investments and financing decisions. This will not exhibit a systematic pattern over time. Miller and Modigliani (1961) argued that the firm's value is determined only by its basic earning power and its business risk. The clientele effect also provides an alternative argument for the irrelevance of dividend policy, at least when it comes to valuation. In summary, if investors migrate to firms that

pay the dividends that most closely match their needs, no firm's value should be affected by its dividend policy.

According to him the current year earnings and previous year dividends influence the dividend payment pattern of a firm. Fama and Babiak (1968) studied the determinants of dividend payments by individual firms during 1946-64. The study concluded that net income seems to provide a better measure of dividend than either cash flows or net income and depreciation included as separate variables in the model. Baker, Kent & Garry and Powell, (2000) surveyed 318 New York stock exchange firms and concluded that the major determinants of dividend payments are anticipated level of future earnings and pattern of past dividends.

1.1.4 Dar Es Salaam Stock Exchange

The Dar es Salaam Stock Exchange (DSE) is a stock exchange located in Dar es Salaam, the largest city in Tanzania. It was incorporated in September 2006 and trading started in April 2008; it is a member of the African Stock Exchanges Association. The exchange is open five days a week, from Monday through Friday. The trading days are weekly from Monday to Friday, starting from 10.00 am to 12.00 noon. The activities of the exchange are monitored and supervised by the Capital Markets and Securities Authority (CMSA). The DSE operates in close association with the Nairobi Securities Exchange in Kenya and the Uganda Securities Exchange in Uganda. Plans are underway to integrate the three to form a single East African bourse.

Total dividend of TZS 30.4 billion will be paid out, higher than TZS 26.1 billion paid in year 2012 with percentage increase of 17% that makes Earnings per share 39.00, Price earnings ratio TZS 7 and Dividend yield of 5%. Dividend is paid directly to shareholders bank accounts; through M-Pesa, Airtel Money and Tigo Pesa for those who have issued instructions; and through dividend cheques issued and payable at CRDB Bank Plc branches.

Tanzania Posts Corporation makes the payment through Post Giro Services in areas where there is no branch of CRDB Bank. CMSA's appropriate market structure study examined both scenarios. Both local surveys and experience from other countries pointed in the direction of EGM. It was found that the ad-hoc, not organized and not formalized structure of OTC is not suitable for Tanzania. Surveyed potential issuers and investors were extremely uncomfortable with the lack of organization and formalization of OTC trade. Also, several countries which had experimented OTC driven growth of capital markets, had negative experiences. Many such experiments, in essence failed, primarily because of not having been able to attract issuers and investors; as well as problems caused by fraud, negligence and mismanagement, thus aspects that arose from low levels of formalization and organization that is inherent to OTC markets.

1.2 Research Problem

Dividend policy has been analyzed for many decades, but no universally accepted explanation for companies observed dividend behavior has been established. The relationship between dividend and the value of the share is not clear cut. The financial manager

must understand the various conflicting factors which influence the dividend policy before deciding the allocation of its company's earnings into dividends and retain earnings. Brealey & Myers (2005) described dividend policy as one of the top ten most difficult unsolved problems in financial economics. This description is consistent with Black 1976 who stated that the harder we look at the dividend picture, the more it seems like a puzzle, with pieces that don't fit together. It is noted that researchers have focused mainly on developed markets, while little or no attention has been paid to dividend policy in emerging markets.

Management are in a dilemma about whether to pay a large, small or zero percentage of their earnings as dividends or to retain them for future investments. This has come about as a result of the need for management to satisfy the various needs of shareholders. For instance, shareholders who need money now for profitable investment opportunities would like to receive high dividends now. On the other hand, shareholders who would like to invest in the future will prefer dividends to be retained by the company and be reinvested. Also, in Tanzania dividends are subject to 5% rate of withholding tax whereas capital gains on shares listed on Dar Es Salaam Stock Exchange are exempt from tax. Thus, some shareholders might prefer low dividends to high dividends in order to take the benefits accruing on capital gains.

Dividend policy is one of the most widely researched topics in the field of finance but the question is whether dividend policy affects stock prices still remain debatable among managers, policy makers and researchers for many years. Black (1976) hinted that, "The harder we look at the dividend picture, the more it seems like a puzzle, with pieces that

don't fit together". In over thirty years since then a vast amount of literature has been produced examining dividend policy. Recently, however, Frankfurter et al. (2002) concluded in the same vein as Black and Scholes (1974) that: The dividend "puzzle", both as a share value-enhancing feature and as a matter of policy, is one of the most challenging topics of modern financial economics. Local studies done Local studies done are Mutiso (2011) did a study on relationship between shareholders dispersion, firm size and dividend policy of firms, Malombe (2011) the effects of dividend policy on profitability of SACCOs with Fosas in Kenya. Fama (2001) studied the determinants of dividend payments by individual firms during 1946. The results showed that net income seems to provide a better measure of dividend than either cash flows or net income and depreciation included as separate variables in the model.

Al-Malkawi (2007), observed that dividend payment patterns of firms are a cultural phenomenon, influenced by customs, beliefs, regulations, public opinions, perceptions and hysteria, general economic conditions and several other factors, all in perpetual change, impacting different firms differently, hence we can‘t have a uniform policy for all firms at all times. No known study has been put forward to look at the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange. Motivated by this gap in literature, the study seeks to determine the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange. The study seeks to answer the research question on what is the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange?

1.3 Research Objective

To investigate on the effects of earnings on dividend policy of firms listed at the Dar Es Salaam Stock Exchange

1.4 Value of the Study

Findings of the study will particularly be useful in providing additional knowledge to existing and future institutions the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange and provide information to potential and current scholars on dividend policy and value firm. This will expand their knowledge on the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange and also identify areas of further study. The study will be a source of reference material for future researchers on other related topics; it will also help other academicians who undertake the same topic in their studies.

This study will benefit investors are concerned with the value, which their investment will bring, thus both current and potential investors will be comfortable investing where they are assured of a good return.

Dividend policy is important for investors, managers, lenders and for other stakeholders. It is important for investors because investors consider dividends not only the source of income but also a way to assess the firms from investment points of view. Previous empirical studies have focused mainly on developed economies. The study undertaken looks at the issue from emerging markets perspective by focusing exclusively on

Tanzania Information Technology, FMCG and Service sector respectively. The major objective of this research is to empirically examine rationale for stable dividend payments by finding the effects of earnings on dividend policy of firms listed at the Dar es Salaam stock exchange.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter provides theoretical and empirical information from publications on topics related to the research problem. It summarizes the information from other researchers who have carried out their research in the same area of dividend policy and firm value.

2.2 Theoretical Framework

2.2.1 The Bird-In-Hand Fallacy

Gordon (1963) and Lintner (1962) argued that the required rate of return on equity decreases as the dividend payout is increased. This is because investors are less certain of receiving capital gains that are supposed to result from retaining earnings, than they are of receiving dividend payments. They said that investors value a currency unit of expected dividends more highly than a currency unit of expected capital gains because the dividend yield component is less risky than the capital gains component of return. Modigliani and Miller termed this argument as the Bird in Hand fallacy.

A more sophisticated argument for a relationship between the value of the firm and dividend payout proposed by Gordon and Lintner (1956) is that although the dividend decision cannot change the present value of cash payments to shareholders, it can affect the temporal pattern of payouts. Suppose that investors view distant dividend payments as riskier than current payments, might they not prefer a bird in the hand to two in the

bush? We can represent this argument mathematically by assuming that higher investment rates mean lower current dividend payout, more risk, and therefore an increase in the market rate of return, **p,** as a function of the investment rate, **k.**

A simple example would be to specify the relationship as

$$\rho = \propto + BK^2, B> 0 \ldots\ldots (1)$$

Then we would have

$$\frac{\delta V_0}{\delta K} = \frac{NO1_1 (BK^2 - 2BK + r - \alpha)}{(a + BK^2 - rK)^2} \quad \alpha + BK^2 - rK > 0 \ldots\ldots (2)$$

This function will have a maximum where

$$NO1_1(BK^2 - 2BK + r - \alpha) = 0 \ldots\ldots (3)$$

The risk of the firm is determined by the riskiness of the cash flows from the projects. An increase in dividend payout today will result in an equivalent drop in the ex-dividend price of the stock. It will not increase the value of the firm by reducing the riskiness of future cash flows (Weston & Copeland, 2002).

2.2.2 Dividend Irrelevance Theory

It has been argued that dividend policy has no effect on either the price of a firm's stock or its cost of capital; dividend policy is irrelevant. The principal proponents of this view are MM (1961). They argued that the firm's value is determined by its basic earning power and its business risk. MM argued that the value of the firm depends only on the income produced by its assets, and not how this income is split between dividends and retained earnings. It contends that there are only two components of shareholders returns:

Dividend yield i.e. **D/Po**

Capital gain yield i.e. **(P1/P0)/P0**

The interests of non-investor stakeholders can affect the financial decision-making process of firms, through both explicit and implicit claims on the value of the firm. The value of implicit claims is related to the total risk of the firm. As the firm decreases its ability to honor implicit claims, it becomes riskier to its stakeholders. As noted above, to compensate for this risk, the value of the goods or services that the firm sells is reduced. Implicit claims are more sensitive to changes in the financial condition of the firm than are explicit claims, since a firm can choose to default on its implicit claims without being forced into bankruptcy. If firms have serious cash flow shortages, they will default on implicit claims first, then on explicit claims. Thus, implicit claimants are at the greatest risk.

2.2.3 Clientele Effect Theory

According to this theory, dividend policy is irrelevant in determining the firm's value. It has its foundation in the observation that different groups of stockholders prefer different payout policies. Depending on their tax bracket, stockholders may have preference for cash dividend or retained earnings. Investors with a high need for investment income (cash dividend) would prefer high payout firms while those seeking long-term gains would prefer low payout firms. To the extent that stockholders can shuffle their portfolios, a firm can shift from one payout policy to another and then let stockholders who do not appreciate the new policy sell to investors who do. Frequent switching is however disadvantageous due to inefficiencies caused by brokerage costs, the capital

gains taxes levied on sales, as well as a shortage of new investors willing to take up the stocks. A stock price drop triggered by a sale of stocks by holders dissatisfied with the new payout policy could be permanent if new investors are not found. The new policy may of course attract a larger group of stockholders resulting in a stock price rise. Pettit (1977) found significant evidence of a clientele effect.

2.2.5 Agency Theory

Agency theory suggests that dividends can be used as a means to control a firm's management. Distributing dividends reduces the free cash flow problem and increases the management's equity stake. The question remains why the shareholders would not use debt or share repurchases instead. LaPorta *et al*, (2000) find that in countries with better shareholder rights firms pay proportionally more dividends. Therefore "there is no evidence that in countries with low investor protection, management will voluntarily commit itself to pay out higher dividends and to be monitored more frequently by the market" (Allen and Michaely 2002).

Fudenberg and Tirole (2005) build a model that shows that, when managers are risk-averse and more recent information has a higher weight in assessing their performance, there will be both dividend and earnings smoothing. Another agency problem is that between shareholders and debtholders. The risk that shareholders will expropriate debtholders by paying themselves excessive dividends has led to the often encountered covenants restricting dividend policy in bond contracts. Empirical studies also suggest that firms hold more cash than the minimum stipulated in bond contracts in order to

consolidate their reputation as good quality borrowers. (Kalay 1982). The reputation effect is also supported by the fact that firms in financial distress are reluctant to cut dividends (DeAngelo and DeAngelo 2000).

2.3 Determinants of dividend policy

In addition to inside ownership, outside ownership could also be related to target returns. Shleifer and Vishny (1986) argue that large outside shareholders have greater incentive to engage in costly monitoring of the firm's management regardless of the free-rider problem, and that they cause higher *ex ante* firm value due to a higher likelihood of a takeover. If outsiders effectively monitor and increase *ex ante* firm value through better performance, then lower target returns may result from a high *ex ante* valuation of the target. Even if outside shareholders cannot monitor management, they can share takeover gains with rival management teams in order to replace incumbent management.

Under any of these scenarios and conditional on a takeover occurring, active-outside ownership should be negatively related to target returns. To control for the level of *ex ante* firm value the model specifications include the target's book-to-market ratio, the market-adjusted runup and the level of industry merger activity. These are potentially confounding factors if book-to-market also prices the likelihood of a value enhancing takeover. While high (low) book-to-market could indicate poor (good) performance based on the assets in place, it could also indicate, a low (high) degree of takeover anticipation. Cross holdings in other companies can pose problems in valuation, partly because of the way these holdings are reflected in accounting statements.

2.3.1 Profitability

Amidu (2007) found that dividend policy affects firm performance especially the profitability measured by the return on assets. The results showed a positive and significant relationship between return on assets, return on equity, growth in sales and dividend policy. This showed that when a firm has a policy to pay dividends, its profitability is influenced. The results also showed a statistically significant relationship between profitability and dividend payout ratio. A study by Howatt et al. (2009) also concluded that positive changes in dividends are associated with positive future changes in mean real earnings per share.

Velnampy, (2006) examined the financial position of the companies and the relationship between financial position and profitability with the sample of 25 public quoted companies in Sri Lanka by using the Altman Original Bankruptcy Forecasting Model. His findings suggest that, out of 25 companies only 4 companies are in the condition of going to bankrupt in the near future. He also found that, earning/total assets ratio, market value of total equity/book value of debt ratio and sales/total assets in times are the most significant ratios in determining the financial position of the quoted companies.

2.3.2 Risk

It is necessary to state that dividend policy is a set of corporate rules, regulations and guiding principles that a firm uses to decide on whether to pay dividend to owners (shareholders).The dividend payment decision of firms is one of the main element of corporate financial decisions which is basically served as a benefit to shareholders in

return for the risk of investing their money. Dividend policy is established by taking different factors into considerations that exist within and outside the organization. Fundamentally, these factors may include but not limited to the followings: credit limit, real and financial investment chances and choices, size of the organization, including the company laws or regulations. However, the dividend policy may as well be influenced by earnings management as established by some authors (Moghri & Galogah, 2013).

Ben-Zion & Shalit, (1975) studied the impact of size, leverage and firm's dividend records on the risk of common stock. They selected the 1000 largest US industrial corporations in 1970 as sample and examined the relationship between alternative risk measures with size, leverage and dividend records. The results of their research showed that the firm's size and leverage and dividend have significant relationship with firm's risk measures and are important determinants of firm's risk. They reported that firm's risk has significant negative relationship with both dividend yield and size, but leverage has significant negative impact on firm's risk.

2.3.3 Cash Flow

The conventional measure of dividend policy the dividend payout ratio gives the value of dividends as a proportion of earnings. In contrast, our approach measures the total cash returned to stockholders as a proportion of the free cash flow to equity.

$$\text{Dividend Payout Ratio} = \frac{\text{Earnings per share}}{\text{Dividends per share}}$$

$$\text{Cash to Stockholders to FCFE Ratio} = \frac{\text{Dividends + Equity Repurchases}}{\text{FCFE}}$$

The ratio of cash to FCFE to the stockholders shows how much of the cash available to be paid out to stockholders is actually returned to them in the form of dividends and stock buybacks. If this ratio, over time, is equal or close to 1, the firm is paying out all that it can to its stockholders. If it is significantly less than 1, the firm is paying out less than it can afford to and is using the difference to increase its cash balance or to invest in marketable securities. If it is significantly over 1, the firm is paying out more than it can afford and is either drawing on an existing cash balance or issuing new securities (stocks or bonds).

2.3.4 Growth

According to Baskin, (1989) he used the Gordon growth model for demonstrating this effect. Moreover, he explained that based on the rate of return effect, it is possible that firms with low dividend yield and low pay out to be assessed more valuable than their assets in place due to their growth opportunities. Since forecasts of earning from growth opportunity have more error than prediction of earning from assets in place, companies with low pay out and low dividend yield are expected to have more volatility in their share price. He also proposed that higher dividend yield will lead to higher arbitrage profit because the excess return is subordinate of dividend yield and price discount rate. Baskin also argued that managers can controls the stock price volatility and stock risk by dividend policy and Distribution of dividend at the time of earning announcement may be interpreted as signal about stability of firm.

Dividend Payment Equations

$$DIVt = b0 + b1GRTt + b2SZt + b2CSt + \mu$$

In the liquidation value approach, you are assuming that your firm has a finite life and that it will be liquidated at the end of that life. Firms, however, can reinvest some of their cash flows back into new assets and extend their lives. If you assume that cash flows, beyond the terminal year, will grow at a constant rate forever, the terminal value can be estimated as follows:

2.3.5 Size

Consistent to Allen & Rachim (2006) Australia results (Hussainey et al., 2011) found a significant negative relationship between share price volatility and payout ratio. They also found a negative relationship between share price volatility and dividend yield. Their findings discovered that the payout ratio is the predominant determinant of the share price volatility and size and debt have the strongest relationship with price volatility amongst control variables. Contrary to (Allen & Rachim, 2006), (Hussainey et al., 2011)'s findings showed that a firm's size has significant negative impact on volatility of stock price and firm's size. They also reported a debt has significant positive impact on share price volatility. (Baskin, 1989) proposed that size, earning volatility, debt and growth affect the both share price volatility and dividend policy. The market risk faced by firm can affect the both dividend policy and share price volatility so a control variable as a measure of earning volatility

Additionally, it is possible that size of firm affects the price volatility because small firms usually have less diversification in their activities. Moreover, it is possible that small firms have less information available to investors about their stock market. Another reason for impact of size on share price volatility is that small firms' stock may be more liquid, so their share price can be more volatile than larger firms. Baskin (1989) proposed that firms which have more scatter body of shareholders are more likely to use dividend as a signaling device, so the size can affect the dividend policy too.

2.4 Empirical literature

In his survey paper, Karpoff (1986) stresses that the increase in trading volume caused by public announcements may either be a consequence of different interpretations of the news by investors, or market participants' interpretations are identical, but they start from diverse prior beliefs. Assume that investors are diversely informed and typically differ in terms of the precision of their private prior information. Consequently, their responses to the announced news differ and this leads to an increase in trading volume. Abnormal trading volume, in conjunction with price reactions, may also be caused by noise-traders who revise their portfolios on the basis of recent price changes rather than new information.

Adesola and Okwong (2009), did an empirical study of dividend policy of quoted companies in Nigeria. This study attempt to evaluate the observed dividend policy of a cross section of 27 Nigeria quoted companies using theories tested to explain dividend behavior of those firms. These theories which are several and varied; even contradict

each other and considerable doubt exist as to which theory best represent the observed dividend behaviour of Nigerian firms; hence the need for this study. To carry out this study a more recent data for the period (2006 – 2006) were reviewed and a model with the necessary policy variables constructed. Factor upon which dividend decisions are based are identified and the magnitude of their effect estimated. Our estimation reveals that the traditional factors are significant in explaining and predicting their dividend decision within the period under review. The result provides strong support for the explanatory or predictive power of Lintner's model. Also, factors which attempt to explain variations in share market prices were identified, and the magnitude of their effect estimated. The result confirms that share market price is a representation of market valuation of dividends.

Lintner (1956) did a study on dividends, earnings, leverage, stock prices and supply of capital to corporations and surveyed a number of managers in the 1950's and asked how they set their dividend policy. One firm's policy might pay out 40 percent of earnings as dividend while another company target 50 percent suggesting that different firms have different dividend policies. Practically, dividend are slow to adjust to changes in earnings. An empirical model whereby changes in the rates of dividend are linked to the earning, the target payout and the adjustment rate. He asserted that more "conservative" companies would be slower to adjust to the target payout if earnings increased. The conservative" investors are risk averse and do not desire to take risks. Therefore conservative firms would prefer not to change their dividend policies over time because

of fear of the reactions this will receive from the existing shareholders and the general public.

According to Ongiri, (2002), the dividend policy of the firm will depend on the nature of the shareholders, that is a firm in which most of its shareholders are in high income brackets will prefer a low dividend payout ratio and vice versa. He concludes that since the composition of the shareholders in the firm keeps changing over time the company's dividend policy is also expected to change over time as per the changes in the nature of the shareholders. A firm that is sticks to its payout ratio would have to change its dividend if its earnings changed. But the managers in Linters survey were reluctant to do this. They believed that shareholders prefer a steady progression in dividends. Therefore, even if circumstances appeared to warrant a large increase in their company's dividend they would move only partly toward their target payment. The more conservative the company, the more slowly it would move toward its targets and, therefore the lower would be its adjustment rate.

Ongiri's (2002) study sought to establish the effect of payment of dividends on Kenyan firms quoted in the NSE. The research covered the firms which were in operation for the periods between 1988 and 2008. The research was geared towards the effect of government change on the above two variables as it touched on both the pre-multiparty and post-multiparty era The study found mixed results as dividend payments affected market share prices in different directions from one company to the next. This study's approach differs from previous studies that examined the effect of dividend policies on market share prices. More specifically, this study attempted to examine evidence on three

related questions, that is, how does payout ratio relate to market share prices of listed companies, how does 100% retention and dividend announcement affect market share prices.

Malombe (2011) carried out a study on the effects of dividend policy on profitability of SACCOs with Fosas in Kenya. The purpose of the study was to establish the effects of dividend policy on profitability of SACCOs with FOSAs in Kenya. A descriptive research design was employed in this study. The target population was SACCOs operating FOSAs in Kenya and the population was taken from the SASRA website on random basis. The study focused on thirty (30) SACCOs that has been licensed by SASRA. Secondary data was collected using the financial statements of the SACCOs sampled for the last five years. Regression model was used to establish the causal relationship between two variables, that is, a dependent (Dividend decisions) and an independent variable (profitability). From the above regression models for the five years, the study found out that the facets of dividend policy (dividend yield and dividend payout) affect the profitability of SACCOs. They either influenced it positively or negatively. The study also found out that the coefficient of SACCOs dividend yield varied from positive to negative. The study found out that the companies dividend payout varied in value although it was positive in most cases except for 2009. The study concluded that there is a positive relationship between dividend policy and the profitability of SACCOs with FOSAs in Kenya. The study recommends constant percentage of earnings dividend policy as it creates certainty in the shareholders expectations.

Nikolaos (2005), did a study on the effect of distributed earnings and size of the firm to its dividend policy: some greek data, In a series of studies, concerning the Greek market, Vasiliou & Eriotis test and improve, using a panel of data, the classical study of John Lintner who explains the amount dividend paid by firms using the earnings of the firm plus an adjustment according to the dividend paid the year before. This paper is an extension of Vasiliou & Eriotis' work that test the assumption that firms set their dividend policy not only by the net distributed earnings, but also by the change from the last year's dividend, the change from the last year's distributed earnings and the size of the firm. This model is applied on a panel sample of a large number of firms listed on the Athens Stock Exchange for the period 2006 – 2001. The hypothesis that is tested in this paper is that the dividend at time t depends upon the distributed earnings at time t, the size of the firm and changes in dividend and distributed earnings from the last year (t-1). The empirical results verified the hypothesis that the Greek companies prefer to distribute, each year a rather constant dividend, which they adjust from year to year according to their distributed earnings and size.

Njoroge (2001), in his research on the relationship between dividend payouts and financial ratios in Kenya came up with the conclusion that in making dividend decisions, the most important variable is the return on the asset. The dividend policy was measure using the dividend yield and the dividend payout while return on equity was used as a measure of profitability. Based on the study findings and discussion, the study concluded

that there is a positive but insignificant relationship between dividend policy and the profitability.

2.5 Summary of Literature Review

The theoretical framework built from the literature review in this chapter helps in understanding and reviewing of dividend policies. The major areas which are covered include: types of dividend policies, different dividend theories, and the empirical studies. The next chapter discusses the methodology of the study. It includes the research design, sampling procedures, data collection instruments, data quality control and data analysis procedures.

While many studies have been done on dividend policies very few have sought to establish how they affect market share prices or market value of listed companies. However, many of the study only concentrated on the effect of dividend announcement on market share prices with very few concentrating dividend policies adopted by the companies. The effect of dividend news/announcement and events by using event methodology to analyze the effect of news and events occurring in the company during the year and found strong relationship both for positive and negative news and events on stock prices.

CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction

The research methodology describes what done during the research in technical terms. It shows the phases of the research project. In this chapter, section 3.2 presents the research design, section 3.4 presents the data collection methods techniques section 3.5 presents the proposed data analysis methods.

3.2 Research Design

This study took on a descriptive survey research design. A descriptive survey attempts to describe or define a subject often by creating a profile of a group of problems, people or events through the collection of data and tabulation of the frequencies on research variables or their interaction as indicated by Cooper and schindler (2003). This was a descriptive study where the researchers gathered data from the published financial statements of listed companies at DSE. The study employed both quantitative method through analysis of the financial statements using various models and ratios to provide predominantly quantitative and qualitative data to the study. The data to be used was accessed from the published financial statements of Listed Firms on Dar Es Salaam Stock Exchange.

3.3 Population

The target population in a research study is the total number of individuals in a group or the number of groups that the researchers are intending to work with (Cooper and

Schindler 2001). Cooper and Schindler (2001) terms the population as the total collection of the elements about which the researchers are intending to make their inferences from. In this study, the target population as of October 2013 there are seventeen listed companies on Dar Es Salaam Stock Exchange.

3.4 Data Collection Techniques

The study used secondary data which was obtained from the financial statements of the Listed Firms on Dar Es Salaam Stock Exchange from 2009-2013. Ratio analysis and various models was used to analyze the secondary data collected.

3.5 Data Analysis Techniques Model

Data analysis involves organizing, accounting for and explaining the data; that is, making sense of the data in terms of respondents' definition of the situation noting patterns, themes, categories and regularities (Cooper and Schindler 2001). The dividend payout ratio is regressed against the five explanatory variables: profitability, risk, cash flow, growth and size. In this equation, $Y_{i,t}$ represents the dependent variable in the model, which is the firms' dividend payout policy measured by the dividend payment; $X_{i,t}$ contains the set of explanatory variables in the estimation model; profitability, size of the firm and cash flow of the firms. This was in the quest of correlating dividend payment with factors such as profitability, growth opportunities, cash flow, the firms' size (market-to-book value) and the risks that the firms faces. α_i is taken to be constant over time t and specific to the individual cross-sectional unit i. If α_i is taken to be the same across units, then Ordinary Least Square (OLS) technique for estimating the unknown

parameters in a linear regression model, provides a consistent and efficient estimate of α and β.The panel regression equation is adopted from Adesola and Okwong (2009) study:

$$\mathbf{DIV\ (y) = \alpha_i + \beta_1 PROF_{i,t} + \beta_2 CASH_{i,t} + \beta_3 SIZE_{i,t} + \beta_4 RISK_{i,t} + \beta_5 GROW_{i,t}} + \mu_{i,t} \text{.....(5)}$$

$$(y = \alpha_i + \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_3 + \beta_4 x_4 + \beta_5 x_5 + \mu_{i,t})$$

Where:

α_i, β_1, β_2 β_3 β_4 and β_5 are constants

DIV = Dividend pay-out policy for FIRM i in period t

$$Di = DPS/EPS = \frac{Dividend\ per\ share}{Earnins\ per\ share}$$

PROF = Earnings before interest and taxes/total assets for FIRM i in period t.

CASH = Cash flow; measured as log of net cash flow for FIRM i in period t

SIZE = which was measured by ratio of total sales(revenue) proxied by natural logarithm of total asset i.e. In (total Asset), CS= Capital structure= Debt divided by market value of equity

RISK = Variability in profit for firm

GROW = Growth proxies by market value of equity divided by book value of Assets.

Dividend Payment Equations; $DIVt = b0 + b1GRTt + b2SZt + b2CSt + \mu$

b0, b1 and b2 are regression parameters, DIVt = Dividend payment in year t, DIVt-1 = Dividend payment in year t-1, EARNt = Total earnings in year t, GRTt = Firm growth in year t, SZt = Size of firm in year t, CSt = Capital Structure in year t

μ = the error term for FIRM i in period t.

The study used linear regression model equation and each independent and dependent variables was tested with t and f tests at a confidence level of 95%.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

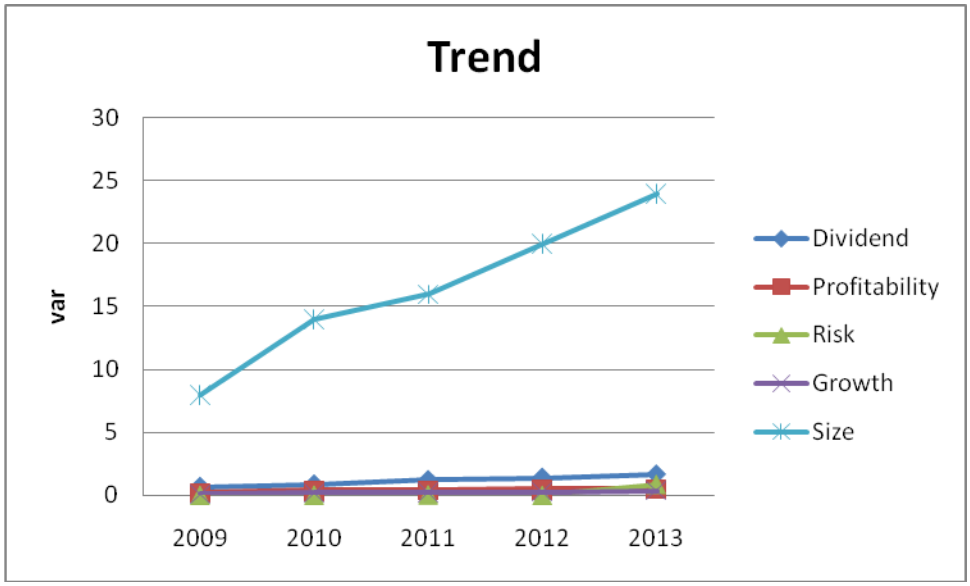
This chapter gives an analysis, presentation and interpretation of data that has been obtained through secondary sources. This data was obtained from the published financial statements of firms listed at the Dar Es Salaam Stock Exchange from year 2009-2013. The data analysis was based on the research objective and analyzed using the regression statistical tool by the assistance of SPSS analytical tool in order to assess the effect of earnings on dividend policy of firms listed in Dar Es Salaam Stock Exchange from year 2009-2013.

4.2 Descriptive Statistics

Table 4.1: Average Performance of firms listed in Dar Es Salaam Stock Exchange

	2009	**2010**	**2011**	**2012**	**2013**
Dividend (ratio in kshs)	0.687	0.876	1.234	1.423	1.675
Profitability	20%	35%	40%	45%	50%
Risk	0.0023	0.021	0.0465	0.654	0.876
Growth	12%	21%	24%	30%	38%
Size	8	14	16	20	24

Figure 4.1: Average Performance of firms listed in Dar Es Salaam Stock Exchange



The table and graph above shows a summary of how the companies registered in Dar Es Salaam Stock Exchange for the past 5 years. Variables vary depending on the year. The table shows that there has been a progressive trend with year 2009 registering the lowest and year 2013 registering the highest on every variable.

4.4 Correlation analysis

Table 4.2: correlation analysis

	profitability	Risk	Cash flow	Growth	Size
profitability	1	0.446	0.06	0.236	0.282
Risk	0.446	1	0.32	0.096	0.03
Cash flow	0.06	0.3	1	0.491	0.242
Growth	0.236	0.096	0.491	1	0.682
Size	0.282	0.03	0.242	0.682	1

The table shows the correlation results of the study on the variables. According to the correlation, the range of the output is between -1 to 1. A positive value indicates that the variables are positively related while a negative value indicates that the variables are negatively related.

4.4 Regression Analysis

The restudy conducted a linear regression analysis to establish the effect of earnings on dividend policy of firms listed in Dar Es Salaam Stock Exchange.

Table 4.3: Regression Model

Model Summary R	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
.407a	.166	.153	1.40018

a. Predictors: (Constant), Profitability, risk, cash flow, growth and size

The study sought to establish the regression model significance, the data of which is presented in Table above. From the regression model, a correlation coefficient value of 0.407 was established. This portends a very good linear relationship or dependence of dividend payout on earnings.. A coefficient of determination (R-square) value of 0.166 was established. Profitability, risk, cash flow, growth and size, according to the model summary Table below explained 17 percent of the variation in dividend policy (R2 = 0.166).

Table 4.4: Analysis of Variance (ANOVA)

	Sum of Squares	**Df**	**Mean Square**	**F**	**Sig.**
Regression	77.417	5	15.58	3.16	.000021a
Residual	390.139	79	4.93		
Total	467.556	85			

Analysis of Variance was used to test the significance of the regression model as pertains to significance in the differences in means of the dependent and independent variables. The ANOVA test produced an f-value of 13.163 which was significant at 0.000021 significance level (p = 0.02). This depicts that the regression model is significant at 95% confidence level; that is, has 2% probability of misrepresentation.

Table 4.5: Regression Coefficients Table

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	.226	1.002		.225	.822
profitability	.066	.011	.382	5.888	.000
Risk	.030	.354	.322	2.654	.122
Cash Flow	.160	.104	.099	1.528	.128
Growth	.100	.093	.420	3.141	.002
Size	.072	.094	.092	.760	.049

$Y = 0.226 + 0.066_{\textbf{prof}} + 0.030_{\textbf{risk}} + 0.160_{\textbf{cash flow}} + 0.100_{\textbf{growth}} + 0.072_{\textbf{size}}$

Results show that all variables studied had a positive effect on dividend policy though it was found to be weak. Profitability (β= .066), risk (β= .030), cash flow (β= .160), growth (β= 300) and size (β= .072). The results of the regression equation below shows that for a 1- point increase in the independent variables, dividend policy was predicted to increase by 0.226 given that all the other factors were held constant. Sig value in the ANOVA table help us to determine if the condition means under study were relatively the same or if they were significantly different from one another the study found out sig value was 0.822. This value was more than 0.000021 hence it can be concluded that there was statistically positive weak significant difference between the condition means.

4.4 Discussion of findings

From the research findings, it was established that earnings has an effect on the firm's dividend policy. The relationship between the two variables was found to be a weak positive. The weak positive relationship indicated that earning influenced dividend policy in the same direction but not to a statistically significant level. A weak positive relationship showed that earnings had very little effect on the dividend policy of firms. 17 firms were analyzed by first collecting data on the earnings and dividend payout of each firm. By the use of regression analysis and use of SPSS software the correlation coefficient of was obtained in order to establish the relationship between the variables under research. Earning accounted for 16.6% of the dividend payout of the firms analyzed.

These results are consistent with Lintner's model supporting the argument that current earnings bear on the dividends to be paid from current earnings. Firms at the DSE pay dividends on outstanding shares at a rate of 45% mostly based on operating earnings per share. Findings were also consistent with those by Adaoglu (2000); Malkawi (2007); Naceur et al (2006); Vasiliou & Eriotis (2003). However, dividend yield and size was insignificant which is inconsistent with Asif et al (2011); Aivazian, (2003) and Li, & lie, (2006). They argued that firms are more likely to raise their dividends if they are large and profitable. This was not the case for companies listed at the exchange based on empirical data. Adaoglu, (2000) realised similar results in turkey and Pandey, (2001) in Malaysia. A negative relationship was returned between dividend yield and payout. This was possibly because high payout of dividends reduced yields for investors. Lastly, size does not matter when making dividend decisions by firms at the exchange.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents discussions of the key findings presented in chapter four, its conclusions based on the findings and recommendations thereto. This chapter will therefore be structured into summary discussions on the findings, recommendations and areas of further research.

5.2 Summary

The study desired to find out the effect of earnings on dividend policy of firms listed in Dar Es Salaam Stock Exchange from year 2009-2013. From the study findings, it is evident that the most critical factors considered by a firm in coming up with a dividend policy are the expected cash flows, risk, profitability, growth and size of the firm. a correlation coefficient value of 0.407 was established. This portends a very good linear relationship or dependence of dividend payout on earnings. A coefficient of determination (R-square) value of 0.166 was established.

Profitability, risk, cash flow, growth and size, according to the model summary from the data analysis, profitability, growth, cash flow, risk and size had a positive impact on the dividend policy. It is therefore imperative from the study that different firms which have adopted different dividend decisions guided by different dividend policies have ended up performing differently financially.

That dividend policy of a given firm is highly affected by numerous variables like , size ,growth , profitability and risk. therefore management of listed companies in Tanzania should focus in moderation of variables as indicated in the study model if they are to realize more dividend for the owners.

5.3 Conclusion

The research study concluded that earnings to some minimal extent, influenced the dividend policy of individual firms. The final correlation coefficient for all variables showed that the relationship between earnings and dividend policy was not strong. Earnings could therefore not be used to predict the dividend policy of individual firms.

The influence of the volatility in earnings was found to be limited however by other factors characterized by the individual firm policies. Some firms that made huge profits ended up issuing a low dividend payout in the five years under review. In most firms the years when a high volatility in earnings was recorded also indicated a lower dividend payout.

The study further concludes that an increase in firms stocks trading volume affected the share price and those investors who wanted current investment income owned shares in high dividend payout firms.

Finally the study concludes that free cash flow caused conflict between management and shareholders and that the executive option plan persuaded management to reduce corporate dividends by an amount that was equal to the option plan.

5.4 Recommendations

Earnings volatility was found to influence firms' dividend payout in different ways. The research found that earnings accounted for 16.6% of divided policy. Further research was found necessary to determine the other specific determinants of dividend policy for individual firms. This was due to the fact that earnings were found not to be the only factor that determined the level of dividend policy which a firm's management agreed upon.

Based on the findings of this research study, the following recommendations are made. First, Organizations should ensure that they have a good and robust dividend policy in place. This will enhance their profitability and attract investments to the organizations. Secondly, directors of corporate organizations should be made to update the records of shareholders including their next-of-kin to avoid a deliberate diversion or undue retention of unclaimed dividend warrants. Due procedures for the recognition and utilization of profit arising from investment of unclaimed dividend should be effected and properly accounted for. Thirdly, a more stringent level condition should be established to compel directors to only invest in profitable ventures, report the utilization of retention earnings through notes to the accounts.

Dividend policy have an effect on the share prices of the firms quoted at Dar Es Salaam Stock Exchange thus, companies (firms) should pay dividends to maintain high share prices. This is continent with the dividend theories of bird-in-hand theory, information signaling effect theory, tax differential theory and agency theory. These theories propose that dividend policy is relevant to the value of the firm; other factors kept constant. It is also recommended that firms should maintain a clear and consistent dividend policy for the dividend policy to affect the value of the firm. Lastly, Government should set up a body that will help to manage unclaimed dividends and also ensure that situations that give rise to such are minimized

5.5 Limitations of the Study

There was a challenge which was encountered during the study. Some Officers from companies that participated in the study were initially reluctant to release information related to Audited accounts and Annual reports making arguments that it was confidential. That reluctance delayed the completion of data collection.

Further, the model may not be reliable due to some shortcoming of the regression models. Due to the shortcomings of regression models, other models can be used to explain the various relationships between the variables. Further, the data was tedious to collect and compute as it was in very raw form. Further the presentation of the data in the different companies was varied which made the data computation even harder.

The other limitation was the end of year accounting activities which some firms undertook after issuing the financial statements in a certain period. These activities being the end of year balance sheet activities ended up distorting the previous information regarding earnings, DPS and EPS declared by a firm before. However, the study made use of the audited financial information that was provided by a firm for the five years under review.

Another limitation was the time taken to do the study. The study was under taken in 17 companies registered in Dar Es Salaam Stock exchange and it took time to gather the data required since the companies are in different locations.

The study uncounted financial constrains since the date was collected in Tanzania where Dar Es Salaam Stock Exchange is located. The major costs were on transportation since we had to travel to and from Tanzania as the study was presented in Kenya.

5.6 Recommendations for Further Studies

The research study covered only five years between 2009 and 2013. Further research can be done on similar study for an extended period of time to ensure that more information is gathered to adequately find the relationship between the two variables under research.

Firms that are not listed under the Stock Exchange market should also be researched on in regards to earning and dividend policy in order to also understand the relationship between the two variables among firms not listed on the Stock Exchanges market.

A similar study can also be done on firms operating in our neighboring countries i.e. Uganda, Kenya, Rwanda and Burundi to confirm if the same pattern is depicted.

Our study concentrated on only five variables which are dividend, profitability, risk, growth and size. The study therefore recommends further research to be done on other variables that were not included in our research such as liquidity, cash flow and corporate tax.

REFERENCES

Adesola W. A. And Okwong A. E. (2009). An empirical study of dividend policy of quoted companies in Nigeria. *Global journal of social sciences*. 8, 1.

Aivazian, V., Booth, L. and Cleary, S., (2003). Do Emerging Market Firms Follow Different Dividend Policies From U.S. Firms. *Journal of Financial Research*, 26(3), 371-387.

Allen P., and Michaely G. H., (2002), Dividend policy and its Relationship to Investment and Financing Policies: Empirical Evidence, *Journal of Business Finance and Accounting* 12, 531-542.

Allen, D. E., & Rachim, V. S. (2006). Dividend policy and stock price volatility: Australian evidence. *Applied Financial Economics, 6*(2), 175-188.

Allen, F., Bernardo, A.E., & Welch, I. (2000). A theory of dividends based on tax clienteles. *Journal of Finance*, 55, 2499–2536.

Al-Malkawi, J. (1959). *Dividends, Earnings and stock prices, Review of economics and statistics* 41. 99-105

Amidu, M. (2007). *How does dividend policy affect performance of the firm on Ghana stock Exchange*. Investment Management and Financial Innovations, 4(2), 104 – 112.

Amihud, Y., & Murgia, M. (2007). Dividends, taxes, and signaling: Evidence from Germany. *Journal of Finance*, 52, 397–408.

Arif, A., Abrar, A., Aziz Khan, M., Kayani, F., and Ali Shah., S.Z. (2011). Dividend Policy and Earnings Management: An Empirical Study of Pakistani Listed Companies. *Information Management and Business Review*, 3, (2), 68-77.

Baker, H. Kent, and Garry E. Powell., (2000), Determinants of corporate dividend policy: a survey of NYSE firms, *Financial Practice and education* 9, 29-40

Baskin, J. (1989). Dividend policy and the volatility of common stocks. *The Journal of Portfolio Management, 15*(3), 19-25.

Ben-Zion, U., & Shalit, S. S. (1975). Size, leverage, and dividend record as determinants of equity risk. *The Journal of Finance, 30*(4), 1015-1026.

Best, R.J., & Best, R.W. (2001). Prior information and the market reaction to dividend changes. *Review of Quantitative Finance and Accounting*, 17, 361–376.

Black, F. (1976), The Dividend Puzzle, *Journal of Portfolio Management*, 2. 2, 5–8.

Black, F., and Scholes M. (1974), The Effects of Dividend Yield and Dividend Policy on Common Stock Prices and Returns, *Journal of Financial Economics,* 1, 1-22.

Brealey, R., & Myers, S. (2005), *Principles of Corporate Finance.* London: McGraw-Hill, pp. 155–167.

Chawla, D., & Srinivasan, G. (1987). Impact of dividend and retention on share price: An econometric study. *Decision Journal*. 137-140.

Cooper D. and Schindler P. (2001), Business research Methods, McGraw Hill, New York.

Cooper F. and schindler D. (2003). *Research methods, quantitative and qualitative approaches.* Nairobi: ACTS Press.

Curran, W. S. (1970). *Principles of Financial Management*. New York: McGraw-Hill.

DeAngelo, H.L., DeAngelo, L., & Skinner, D. (2000). Special dividends and the evolution of dividend signaling. *Journal of Financial Economics*, 57, 309-54.

Fama, E. (2001). Dividend policy, an empirical analysis. *Journal of the American statistical association* 63. 324

Fama, E.F., & French, R. (2008). Taxes, financing decisions and firm value. *Journal of Finance,* 53, 819.

Fama, E.F., Fisher, L. Jensen, M.C. & Roll., R. (1969). The Adjustment of Stock Prices to New Information. *International Economic Review*, 10, 1-2.

Fama, Eugene and Harvey Babiak, 1968, Dividend policy: an empirical analysis, *Journal of the American Statistical Association* 63, 1132-1161.

Frankfurter, G.M., & Wood, B.G. (2002). Dividend policy theories and their empirical tests. *International Review of Financial Analysis*, 11, 111–138.

Fudenberg P., and Tirole R. R., (2005). Dividend Announcements, Security Performance, and Capital Market Efficiency, *Journal of Finance* 27, 993-1007.

Gitman, J.L. (2008). *Money and financial markets*. United States; Harper and Row Publishers.

Gordon, Myron J., 1963, Optimal Investment and Financing Policy, *Journal of Finance* 18, 264-272.

Gordon, Myron J., and Eli Shapiro, (1956), Capital Equipment Analysis: The Required Rate of Profit, *Management Science* 3, 102-110.

Holder, M.E., Langrehr, F.W., & Hexter, L. (2008). Dividends policy determinants: An investigation of the influences of stakeholders' theory. *Financial Management Journal,* 27, 73.

Horne, V.J. (2007). *Financial management and policy* (9thed). New Delhi: Prentice-Hall India Private Limited.

Horne, V.J. (2008). *Fundamentals of financial management* (13th ed). New Delhi: Prentice Hall India Private Limited.

Howatt, B. et al. (2009). Dividends, earnings volatility and information. Applied Financial Economics, 19(7), 551 – 562.

Hussainey, K., Mgbame, C. O., & Chijoke-Mgbame, A. M. (2011). Dividend policy and share price volatility: UK evidence. *Journal of Risk Finance, The, 12*(1), 57-68.

Jensen, M.C. (1986). Agency costs of free cash flow, corporate finance and takeovers. *American Economic Review*, 76, 323–329.

John, K., & Lang, L. (2001). Insider trading around dividend announcements: theory and evidence. *Journal of Finance*, 46(4), 1361-89.

Kalay, I. G., (1982), Dividends and Capital Asset Prices, *Journal of Finance* 37, 1071-1086.

Kania, S.L., & Bacon F.W. (2005). What factors motivate the corporate dividend decisions? *ASBBS E-Journal, 1(1),* Longwood University, VA.

Karpoff, J.M. (1986). A theory of trading volume. *Journal of Finance*, 41, 1069–1087.

Kim, O., & Verrecchia, R.E. (2001). Trading Volume and price reactions to public announcements. *Journal of Accounting Research*, 29, 302–321.

Knott, G. (2004). *Financial management* (4th ed). London: Palgrave Macmillan.

Laffie, L.S. (2004). Time to distribute corporate earnings? Taking advantage of the lower tax rate on dividends received. *Journal of Accountancy*, 197(76).

Lang, L.H., & Litzenberger, R.H. (1989). Dividend announcements: Cash Flow signaling vs. free cash flow hypothesis. *Journal of Financial Economics*, 24, 181–191.

LaPorta, P. Short, Helen, Hao Zhang, and Kevin Keasey, (2000), The Link Between Dividend policy and Institutional Ownership, *Journal of Corporate Finance* 8, 105-122.

Lasher, R.W. (2007). *Practical financial management*. New York: West Publishing Company.

Lease, Ronald C., Kose John, Avner Kalay, Uri Loewenstein, and Oded H. Sarig, (2000). *Dividend Policy: Its Impact on Firm Value* (Harvard Business School Press, Boston, Massachusttes).

Lintner, J. (1956). Distribution of incomes of corporations among, dividends, retain earnings and taxes. *American Economic Review*, 46(2).

Lintner, J., (1962), Dividends, Earnings, Leverage, Stock Prices and Supply of Capital to Corporations, *The Review of Economics and Statistics* 64, 243-269

Malombe E. (2011), effects of dividend policy on profitability of SACCOs; Fosas in Kenya, *Unpublished MBA Project*, University of Nairobi.

Mick, A.C. & Bacon, F. (2003). The determinants of the dividend policy decision. *Academy of Accounting and Financial Studies Journal*, 8(1).

Miller, M. H., & Modigliani, F. (1961). Dividend policy, growth, and the valuation of shares. *Journal of Business*, 34, 411-433.

Miller, M.H., & Rock, K. (1985). Dividend policy under asymmetric information. *Journal of Finance*, 40, 1031–1051.

Moyer, R.C., McGuigan, J.R. & Kretlow, W.J. (2002). *Contemporary Financial Management* (5thed). St. Paul: West Publishing Company.

Mugenda, M.O., & Mugenda, G.A. (2003). *Research methods, quantitative and qualitative approaches.* Nairobi: ACTS Press.

Mutai, B.K. (2001). *How to write standard dissertation; A systematic and simplified approaches*. New Delhi: Thelly Publications.

Mutiso, F.K. (2011). *The relationship between shareholders dispersion, firm size and dividend policy of firms quoted at NSE.* Unpublished MBA project, University of Nairobi.

Myron, G.J. (1963). *The investment, financing and evaluation of corporation*. Richard D: Irwin Publications. Nation Newspaper 11th January 2007

Nikolaos E., (2005), The effect of distributed earnings and size of the firm to its dividend policy: some greek data, *International Business & Economics Journal.* Volume 4, Number 1

Njoroge W. (2001). The Relationship between Dividend Payments and Financial Ratios in Kenya, *Unpublished MBA Project*, University of Nairobi.

Ongiri, A.O. (2002). An analysis on the effect of dividend payout on market price per share for quoted companies in Nairobi Stock Exchange. *Unpublished Master's Thesis*, Kenyatta University.

Pandey, I.M. (2005). *Financial management* (9thed). New Delhi: Vikas Publishing House PVT Limited.

Pearl, J. (2000). *Causality: Models, Reasoning, and Inference.* London: Cambridge University Press.

Pettit, J. A., 1977, Evidence of Tax-Clientele-Related Trading Following Dividend Increases, *Journal of the American Taxation Association* 23, 1-21.

Pradhan, R.S. (2003). Effects of dividends on common stock prices: The Nepalese evidence. *Research in Nepalese Finance*. 1-13.

Ross A.S., Westerfield, R.W., & Jaffe, J. (2005). *Corporate finance*, (7thed). Boston: Irwin/McGraw-Hill.

Shapiro, A.C. (2000). *Modern corporate finance*. New York: Macmillan Publishing Company.

Shleifer, G., and Vishny T., 1986, Taxes, Dividend Yields and Returns in the UK Equity Market, *Journal of Banking and Finance* 22, 405-423.

Teoh, S.H., Welch, I., Wong, T.J., (2008). Earnings management and the underperformance of seasoned equity offerings. *Journal of Financial Economics* 50, 63–99.

Velnampy.T (2006), An Empirical Study on Application of Altman Original Bankruptcy Fore-Casting Model in Sri Lankan Companies", M- Infiniti, Journal of Management, Sai Ram Institute of Management, Sai Ram Engineering College, India, Vol 1, issue 1, April – September.

Weston, P. S, and Copeland T. S, 2002, Signaling, Investment opportunities, and Dividend Announcements, *Review of Financial Studies* 8, 995-1018

Appendices I: Dar Es Salaam Stock Exchange Companies performance

		2009	2010	2011	2012	2013
TOL Gases Ltd	Earnings	3.01	3.45	4.21	4.69	4.72
	Dividends	1.20	1.32	1.48	41.64	1.76
	Payout ratio	40%	38%	35%	35%	37%
Tanzania Breweries Ltd	Earnings	2.33	1.98	2.12	2.12	2.04
	Dividends	0.30	0.80	1.48	1.64	1.76
	Payout ratio	13%	40%	70%	77%	86%
Tanzania Tea Packers Ltd.	Earnings	0.15	1.82	1.17	0.25	(0.63)
	Dividends	0.40	0.40	0.40	0.40	0.10
	Payout ratio	267%	22%	34%	160%	-16%
Tanzania Cigarette Co. Ltd	Earnings	1.01	1.35	0.63	1.17	1.04
	Dividends	0.05	0.04	0.03	0.07	0.73
	Payout ratio	5%	3%	5%	6%	70%
Tanga Cement Co. Ltd	Earnings	1.34	2.14	0.36	(2.99)	0.54
	Dividends	0.60	0.60	0.60	0.30	0.20
	Payout ratio	45%	28%	167%	-10%	37%
Swissport Tanzania Ltd	Earnings	41.43	1.12	1.54	2.00	2.50
	Dividends	1.34	1.36	1.36	1.36	1.36
	Payout ratio	3%	121%	88%	68%	54%
Tanzania Portland Cement Co. Ltd.	Earnings	4.09	5.65	4.89	6.64	4.82
	Dividends	0.29	0.58	1.09	1.00	1.96
	Payout ratio	7%	10%	22%	15%	41%
Dar es Salaam Community Bank Ltd	Earnings	-0.39	2.10	2.32	2.38	2.59
	Dividends	1.05	1.06	1.06	1.06	1.12
	Payout ratio	-269%	50%	46%	45%	43%
National Microfinance Bank	Earnings	2.95	(10.64)	(0.73)	(2.96)	1.41
	Dividends	1.28	1.28	0.80	0.15	0.00
	Payout ratio	43%	-12%	-110%	-5%	0%
CRDB Bank	Earnings	7.11	4.18	0.74	(0.21)	0.22
	Dividends	0.85	1.00	1.00	0.85	0.40
	Payout ratio	12%	24%	135%	-405%	182%
Precision Air Services Plc	Earnings	2.25	(5.96)	(3.05)	(1.76)	(0.62)
	Dividends	1.00	0.75	0.00	0.00	0.00
	Payout ratio	44%	-13%	0%	0%	0%
Maendeleo Bank Plc	Earnings	2.21	0.37	(0.98)	(0.52)	0.42

	Dividends	0.80	0.80	0.60	0.60	0.60
	Payout ratio	36%	216%	-61%	-115%	143%
Swala Gas and Oil	Earnings	1.22	1.75	2.00	2.10	1.03
	Dividends	1.25	1.27	1.29	1.30	1.33
	Payout ratio	102%	73%	65%	62%	129%
Kenya Airways	Earnings	4.61	6.21	5.35	4.86	4.87
	Dividends	1.34	1.23	1.43	1.76	1.22
	Payout ratio	29%	20%	27%	36%	25%
East African Breweries	Earnings	6.23	4.54	3.87	7.65	6.54
	Dividends	0.278	0.978	0.411	1.111	0.431
	Payout ratio	4%	22%	11%	15%	7%
National Media Group	Earnings	4.64	3.23	4.44	5.33	3.22
	Dividends	0.415	0.233	0.338	6.023	0.353
	Payout ratio	9%	7%	8%	113%	11%
African Barrick Gold	Earnings	6.76	5.43	5.44	4.32	4.65
	Dividends	0.305	0.365	0.194	0.247	0.176
	Payout ratio	5%	7%	4%	6%	4%