THE DETERMINANTS OF DIVIDEND POLICY:

EVIDENCE FROM MALAYSIAN FIRMS

BY

AYMAN I. F. ISSA

MASTER OF SCIENCE (FINANCE)

UNIVERSITI UTARA MALAYSIA

JUNE 2012
THE DETERMINANTS OF DIVIDEND POLICY: EVIDENCE FROM MALAYSIAN FIRMS

A thesis submitted to the Postgraduate Studies Othman Yeop Abdullah Graduate School of Business (Division of Finance)
In partial fulfillment of the requirements for the degree Master of Science (Finance)
University Utara Malaysia

BY/ AYMAN I. F. ISSA

MASTER OF SCIENCE (FINANCE)
UNIVERSITI UTARA MALAYSIA

JUNE 2012

AYMAN I. F. ISSA, 2012. All Rights Reserved
DECLARATION

I hereby declare that the thesis is based on my original work except for quotations and citations that have been duly acknowledged.

I also certify that the substance of this project paper has never been submitted for any degree and is not currently being submitted for any other qualifications.

Ayman I. F. Issa

808816

Othman Yeop Abdullah Graduate School of Business

University Utara Malaysia

06010 Sintok

Kedah

June, 2012
PERMISSION TO USE

In presenting this thesis as a part of the requirements for Master of Finance (MSCs) from University Utara Malaysia, I agree that the university library make it freely available for inspection. I further agree that permission of copying of this thesis in any manner, in whole or in part, for scholarly purposes may be granted by my supervisor Prof. Dr. Asish Saha or, in his absence, by the Dean of Othman Yeop Abdullah Graduate School of Business. It is understood that any copying or publication or use of this thesis or parts thereof for financial gain shall not be allowed without my written permission. It is also understood that due recognition shall be given to me and University Utara Malaysia for any scholarly use which may be made of any material from my thesis.

Requests for permission to copy or to make other use of materials in this thesis, in whole or in part should be addressed to:

Dean

Othman Yeop Abdullah Graduate School of Business

University Utara Malaysia

06010 Sintok

Kedah Darul Aman
ACKNOWLEDGEMENTS

In the name of Allah, the Most Gracious and Most Merciful

To begin with praising and glorifying of Allah for allowing me to complete this paper. And a lot of praise for glorified Allah to spirit me up as well as inspiring me to figure out all problems that I faced.

After that, I thank very much my parents to educate, motivate and guide me to reach me for the stars and learning me there aren’t impossibilities in this life once you depend entirely on merciful Allah.

My love to my siblings namely Mohammad, Mohand, Ala’, Monera, and my lovely Batool to stand by me and making me feel that I’m not in homesickness.

Finally, I’d like to express my deep and sincere gratitude to my supervisor Prof. Asish Saha for his guidance, support and advice for the completion of this dissertation.
ABSTRACT

The aim of this study is to investigate the relationship between dividend payout ratio in Malaysian firms with profitability, size, growth opportunities, free cash flow, business risk and market to book value. The paper used a sample of 284 firms listed on the Kuala Lumpur Stock Exchange (KLSE) from seven sectors viz., Consumer Products, Industrial Products, Construction, Finance, Technology, Properties, and Telecommunication. In order to decipher the relationships as stated above, multivariate regression analysis is used to test the hypotheses. The study found that at the pooled data level for All sectors, free cash flow, return on assets, return on equity, earning per share, market to book value and market capitalization have significant positive correlation with dividend payout ratio. The variable Beta, however, has a strong negative correlation with dividend payout ratio. The findings however differ from sector to sector; results reflect that Market capitalization; Beta, ROA and ROE are the common variables which have influence on DPR across various sectors except in technology sector where as the variable Market capitalization is not significantly associated with DPR. Similarly, ROA, which is significant determinant variable of DPR in four sectors like Construction, Consumer Products, Properties and Telecommunication Sector, it has no influence on the dividend payout ratio of the companies in the Industrial, Technology and Finance sectors.
# TABLE OF CONTENTS

DECLARATION........................................................................................................................................ iii

PERMISSION TO USE .......................................................................................................................... iv

ACKNOWLEDGEMENTS ....................................................................................................................... v

ABSTRACT .............................................................................................................................................. vi

CHAPTER ONE ....................................................................................................................................... 1

INTRODUCTION .................................................................................................................................... 1

1.1 Background of Study ...................................................................................................................... 1

1.2 Problem Statement ........................................................................................................................ 4

1.3 Research Objectives ..................................................................................................................... 5

1.4 Research Questions ....................................................................................................................... 5

1.5 Significance of Study ..................................................................................................................... 6

1.6 Scope of Study ............................................................................................................................... 7

1.7 Organization of Study ................................................................................................................... 8

CHAPTER TWO ..................................................................................................................................... 9

LITERATURE REVIEW ......................................................................................................................... 9

2.1 Introduction .................................................................................................................................... 9

2.2 Dividend policy theories ............................................................................................................... 9

2.2.1 MODIGLIANI AND MILLER THEORY ................................................................................. 9

vii
2.2.2 CLINTELE EFFECT ........................................................................................................... 10

2.2.3 SINGALING THIEORY .................................................................................................... 11

2.2.4 BIRD IN THE HAND THEORY ......................................................................................... 12

2.3 Related Empirical Studies ............................................................................................... 14

2.3.1 Profitability ......................................................................................................................... 14

2.3.2 Firm Size ............................................................................................................................ 17

2.3.3 Growth Opportunities ....................................................................................................... 19

2.3.4 The Free Cash Flow .......................................................................................................... 20

2.3.5 Beta “Business Risk” ........................................................................................................... 21

2.3.6 Market to Book Value ......................................................................................................... 22

2.4 Conclusion ............................................................................................................................. 22

CHAPTER THREE .................................................................................................................... 23

METHODOLOGY ....................................................................................................................... 23

3.1 Introduction ........................................................................................................................... 23

3.2 Research Framework ............................................................................................................. 23

3.3 Hypotheses Development .................................................................................................... 25

3.3.1 The dependant variable ..................................................................................................... 25

3.3.2 The independent variables ............................................................................................... 25

3.4 Research Design .................................................................................................................... 31

3.4.1 Data Collection ................................................................................................................... 31
3.4.2 Multiple Regressions and Measurements .............................................. 33

3.5 Data Analysis ............................................................................................................. 35

3.5.1 Descriptive Analysis .......................................................................................... 35

3.5.2 Correlation analysis ............................................................................................ 35

3.5.3 Multiple Linear Regression Analysis ................................................................. 36

3.6 Summary ..................................................................................................................... 36

CHAPTER FOUR ............................................................................................................. 37

ANALYSIS AND FINDINGS ......................................................................................... 37

4.1 Introduction ................................................................................................................ 37

4.2 Descriptive Statistics ............................................................................................... 37

4.3 Correlations Analysis ............................................................................................... 49

4.4 Multiple Linear Regression Analysis ....................................................................... 52

4.5 Discussion .................................................................................................................. 55

4.6 Conclusion .................................................................................................................. 56

CHAPTER FIVE ............................................................................................................. 58

CONCLUSION ................................................................................................................. 58

5.1 Introduction ................................................................................................................ 58

5.2 Summary of observations ....................................................................................... 58

5.3 Limitation of the Study ............................................................................................. 60

5.4 Recommendations for future Research ................................................................. 60
REFERENCES .................................................................................................................. 62

LIST OF TABLES .............................................................................................................. 69

LIST OF FIGURES .............................................................................................................. 71

LIST OF ABBREVIATIONS ............................................................................................. 72

Appendix ........................................................................................................................... 73
CHAPTER ONE

INTRODUCTION

1.1 Background of Study

Since early days of the development of the theory of corporate finance, dividend payout decision of the corporate sector has been a subject of debate in the literature. Role of agency cost, taxation, and transaction cost etc. on dividend decisions continue to draw the attention of researchers. Many models were developed by researchers across the globe to identify factors that drives dividend decisions by companies; findings of these studies varied widely from country to country. Identification of driver variables of dividend payout ratio in an emerging market like Malaysia is more challenging.

Ling, et al (2008) defines dividend payout as distributions of retained earnings to the investors “Shareholders” based on their proportionate ownership. Dividends are usually paid in cash, but sometimes paid in stock or other means. Firms always look for an optimal dividend policy, among others to reach equilibrium among current dividend, future growth, and maximize firm’s stock price.

Miller and Modigliani, in their seminal paper in 196, developed the dividend irrelevance hypotheses and argued that given perfect capital markets, the dividend decision does not
The contents of the thesis is for internal user only
REFERENCES


