Dividend Policy and Ownership Pattern- A Study of Corporate Indian Firms

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ABSTRACT

The ownership pattern are distinctive by large Shareholder and may influence the dividend payout in different manner. In corporate finance the agency problem i.e. a conflict between company management and companies shareholder has constantly been consider as potential weakness. The main purpose in this paper is to study the impact of ownership pattern on dividend policy of the selected company Listed at BSE 500. Since dividend policy is affected by many other variables, we have taken debt equity ratio, net profit ratio and cash flow as controlling variables in the study. The data has been extracted from Bombay stock exchange and company website. The multiple regression analysis has been used to study the effect of share holding pattern on dividend policy. The result revels that 4 % of variation has been explained by the independent variables (promoters, foreign institutional shareholding and institutional shareholding).

Keywords: *Dividend policy, Promoters Shareholding, Institutional Shareholding, Foreign Institutional Shareholding*

Introduction

Dividend policy is the set of guidelines a company uses to decide how much of its earnings it will payout to shareholders. The ownership structure of the Indian companies is distinct from the other countries like USA and UK . In case of India, large shareholders i.e. promoters, directors and corporate have enough rights and potential to influence the financial decision of the company's other then small investors . In the current scenario the various research has been done on the dividend policies of the companies but hardly very few literature are available to see the relationship between Shareholding pattern and Dividend payout. In order to fill up the research gap this paper has proposed to give a solution for the following question for example, does shareholding pattern in a corporate matters for dividend payout? In existing theories Rozeff 1982 argues that payment of dividend yield provide indirect control benefit where shareholder are not engaged energetically in observing the performance of the corporate firm. Easter Brook (1984) argues that corporate firm pay dividend to solve the agency problem arising from separation of ownership and control in a firm with diffused ownership. Jensen (1986) makes a similar argument that manager have their own motive to increase the firm beyond its standard size because increases in resources under their control leads to increase in their incentives. Hence manager could find suboptimal investment that benefit themselves but reduce shareholder wealth.

Literature Review

The literature review concerning to factors affecting dividend policy lies in the well-known paper of Lintner (1956) where he discovered that it is the changes in the earnings and the existing dividend rate are the essential determinants of dividend policy of the firms. After this, another well-known paper came into existence which belongs to Modigliani and Miller (1961). They proved that in the presence of perfect capital market, the dividend decision or the dividend policy of any firm is irrelevant and does not affect the value of the firm.

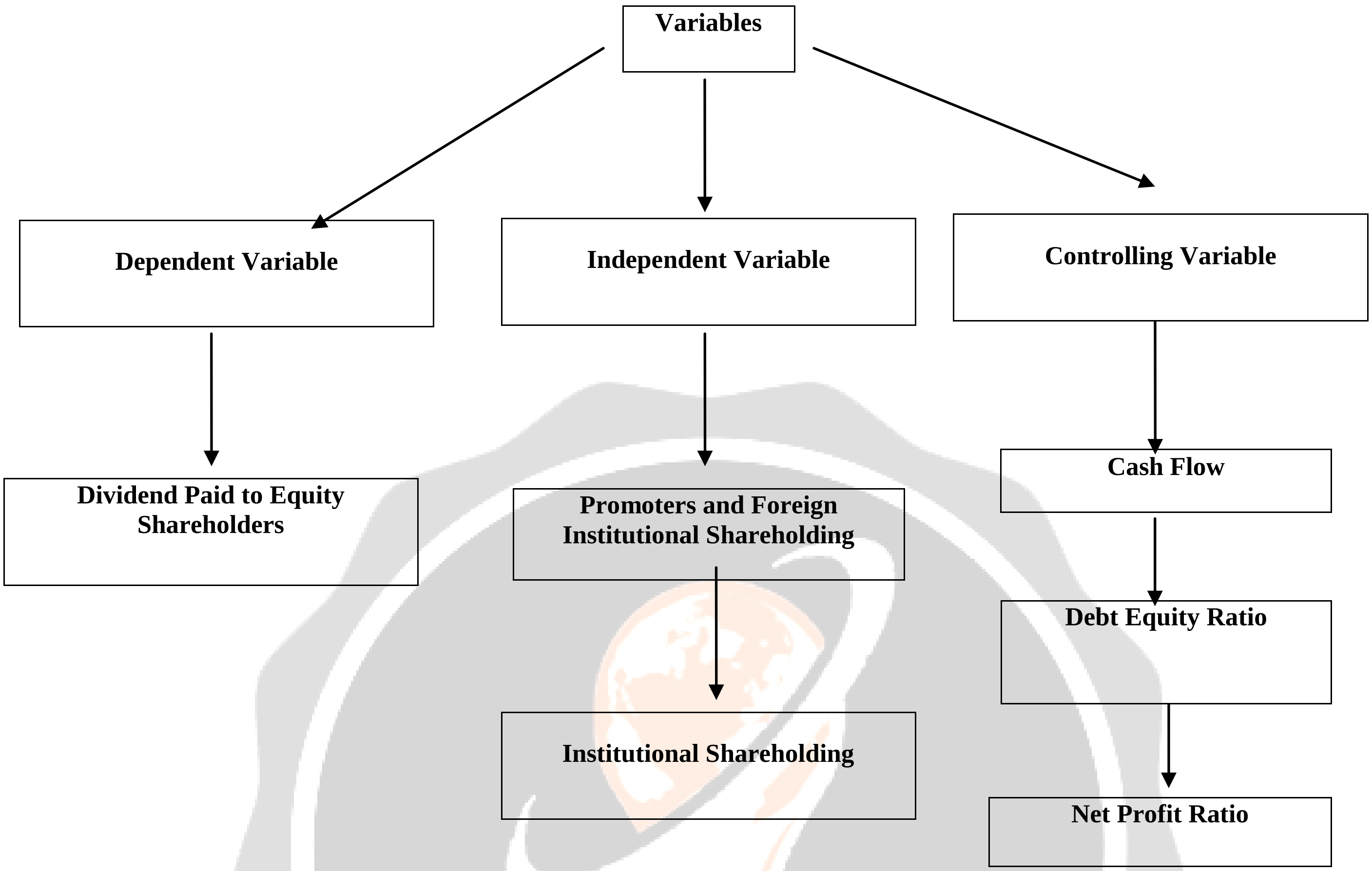

Fig. 1 Factors influencing Dividend payout

Rozeff (1982) had commenced the acceptance of agency cost in dividend determinant. He tested the agency theory of Jensen and Meckling (1976) by building a model of optimal dividend payout in which increase in dividends led to decrease agency costs, but raise transaction costs. He demonstrates that dividend payout is negatively related to the percentage of stock held by insiders. Jensen et al., (1992) examined the Joint Determinants of dividends insider ownership of stock and leverage. They argues that dividend is only means of minimizing the inconsistency of interest between Shareholder and manager. After controlling for growth prospects, investment opportunities, differential profitability and they found that dividend have adverse affect to leverage and insider holding.

Dempsey and Laber (1992) reported that the dividend yield is negatively related to the proportion of stock held by insiders and positively related to the number of common shareholders within the firm. Noronha et al., (1996) examined the relationship between agency cost variables and dividend payout ratios, segmented by the level of the firm's growth opportunities. For firms with low growth opportunities, they report a positive relation among the dividend payout ratio, the presence of outside block holders, and the level of executive incentive compensation

Short et al., (2002) conduct a study considered the first example of using well established dividend payout models to examine the potential association between ownership structure and dividends policy. By using dividend models of Lintner (1956); Fama and Babiak (1968), conclude that a positive association between dividend payout policy and institutional ownership may go beyond increasing the dividend payout ratio. They also found some evidence to support a negative association between dividend payout policy and managerial ownership.

Gugler (2003) used OLS technique to examine the association between dividend payment and ownership control structure. He used a panel of 214 non-financial Australian firms for the year 1991 to 1999. The result of his study stated that state owned firms were occupied in dividend smoothing whereas family controlled firms were not involved for the same. Besides, the state owned firms were most indisposed and family owned firms were keen to cut dividends. The research also experienced that firms with low growth opportunities optimally expel cash irrespective of who controls the firm.

Research Methodology

The research is diagnostic and empirical in nature and uses secondary data from companies balance sheet which is available in bseindia.co.in The period of the study is from Jan 2009 to Dec 31, 2013.Researcher include the sample of those companies that had continuously paid dividend during the study period. Financial Institution/Finance companies ,Government owned companies have been excluded .The sample has consider only those companies which have paid final cash dividend every year And have data on shareholding pattern and other controlling variables for the period of 2009-2013 (both inclusive year).Thus this process gave final sample of 30 companies which provide information as per requirement.

Table 1. Description of variables

Dependent Variables	Dividend paid to equity shareholders as a percentage of Profit after Tax represents the company's dividend policy.
Independent Variable	**a) Promoters and Foreign Institutional Shareholding**: It is the percentage of holdings of Indian promoters, foreign promoters and persons acting in concert in a company b) **Institutional Shareholding:** It include the sum of percentage of banks, insurance companies, investment firms, pension funds and other large scale financial institutions.
Controlling Variable	**Cash Flow**: A firm facing liquidity problem is not likely to have high dividend payout. Thus dividend payout is dependent on the availability of cash flows rather than profit as explained by many studies **Debt Equity Ratio**: Debt has adverse affect on amount of dividend paid because corporate firm with high fixed charges pay less dividend to avoid cost of external finance. **Net Profit Ratio:** Profitability is positively correlated to dividend payout greater the profit of the firm higher will be the dividend payout.

Analysis of Results

The result analysis shows that Independent variable gives only 4% deviation in dividend policy. The F value is 2.945 which is significant at 5% level of significance ($p > 0.05$). Regression Results (Table 2) shows that all the Independent variable i.e. (FS, IS, PS) are positively related to dividend policy decision and also statistically significant. However Table 2 shows that controlling variable namely cash flow, net profit ratio has less positive relationship with dividend policy and also not statistically significant at 5% level of significance And debt equity ratio have negative association with dividend policy .

Table 2: **Regression Result.**

	β	t value	p-value	F value	R2 change
			0.000	2.945	0.04
Constant		2.483	0.000		
FIIs Shareholding	0.054	2.553	0.000		
Institutional Shareholding	0.051	1.471	0.010		
Indian Promoters shareholding	0.029	2.512	0.000		
Cash Flow	0.000	0.069	0.787		
Debt Equity Ratio	-0.011	-1.177	0.101		
Net profit Ratio	0.005	0.258	0.445		

Conclusion

The present study shows that FIIs holdings has major influence on dividend payout of selected companies ,that shows FIIs holding may be higher for the firm which are profitable and pay high dividend .Institutional shareholding and promoters shareholding shows less positively correlated because of time changing factor on dividend payout. However the controlling variable are also examined to study the relationship between ownership structure and dividend policy without extraneous effect and found that they have impact on dividend policy and not statistically significant. Thus our study depicts that all the independent factor have impact on dividend policy.

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