RELATIONSHIP BETWEEN DIVIDEND YIELD AND FINANCIAL PERFORMANCE OF LISTED FIRMS AT THE NAIROBI SECURITIES EXCHANGE

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Abstract

This study assessed the relationship between dividend yield and financial performance of the listed companies at Nairobi Securities Exchange. Bird in hand theory anchored the study. An explanatory research design was adopted where all the 62 firms listed in Nairobi Securities Exchange (NSE) participated in the study. Secondary data collected from the published financial statements for the years from 2018 to 2020 by use of a data collection sheet was analysed using descriptive statistics and regression analysis. The results indicated that dividend yield had a positive and significant relationship with the performance of the listed firms at NSE. The study recommended that the listed firms should strive to have a sizable amount of the profits accrued by the firm be paid as dividends and that the listed firms should strive to be consistent in their dividend payments.

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1. Introduction

Dividend used by itself is generally understood to mean the distribution of earnings by a company to its shareholders (Hayes, 2022). The history of corporate dividends is dated back to the seventeenth and eighteenth centuries when joint stock trading companies in Holland and Great Britain made the first dividend payment (Frankfurter & Wood, 1997). On the other hand, dividend policy emerged in the nineteenth century since dividends came to be seen as an important source of information (Modigliani & Miller, 1961). This was a result of unreliability and scarcity of available financial data in the market which made investors make investment decisions by assessing the dividend patterns of firms. Dividend yield on the other hand is the financial ratio that measures the amount of cash dividends paid out to shareholders relative to the market value per share (Hayes, 2022). Since the emergence of dividend policy in the 19th century, dividend decisions have remained a thorn in the flesh of many companies globally, regionally, and locally.

The global commodity downturn of 2015-16 forced the Broken Hill Proprietary Limited to slash dividends in 2016 for the first time in 15 years which eventually led to a sharp decline in its share price indicating that dividend pay-out has a greater impact on the share price of the companies which eventually affects their performance (BHP 2016). In Africa, the Maritime Telecommunications network group realized a return of $280m in 2020 in form of dividend from the Nigeria subsidiary which happened in two years where dividends had not been declared. After the news of dividend announcement, the share price closed at 6% higher on that very day (Ajifowoke, 2021). This shows that dividends might potentially have a big and favourable impact on a company's share price. In Kenya, it is opined that dividend pay-out does not affect the performance of insurance companies listed in the Nairobi securities exchange (Murimi & Mungai, 2021).

The nature of the association between dividend pay-out and the financial performance of the firm has faced unresolved debate by researchers for a long period of time (Dada et al., 2015). This has remained a controversial problem in the corporate world despite

various studies being done in the area of interest. Black (1976) noted, "the harder we look at the dividend picture, the more it seems like a puzzle with pieces that just don't fit together". In Kenya, the firms listed at the NSE play a critical role in economic growth (Musyoka et al., 2018). Kanyatta and Kagiri (2017) revealed that the stock market development contributes 46.1 percent of the economic growth in Kenya. The NSE 2021 study states that the exchange supports economic growth in Kenya by promoting savings and investment as well as facilitating access to affordable capital for both domestic and foreign businesses. Despite all the benefits, firms at NSE have consistently reported low financial performance which is posing a threat not only to the future of the exchange but also to the future of the companies. Kiuva (2020) revealed that NSE extended suspension on trading of two firms, that is Mumias Sugar Company and Fashion retailer Deacons East Africa shares. This was as a result of the receivership placed on those firms on September 20, 2019 and November 19, 2018 respectively. Amongst the many reasons for poor performance of those firms is lack of a well-structured dividend payout policy which has consistently made the companies' shares to trade below their real values thus lack of prospective investors. Many studies on dividend have dominated developed countries such as Britain and Istanbul such as the works of Musiega et al, (2013) and Adaoglu (2000) respectively. Few studies done in Kenya at NSE have focused on sectors rather than the entire exchange as it is with the works of Kariuki (2016) and Nekesa et al. (2021) who based their studies on the manufacturing and banking respectively.

2. Literature review

The bird in hand theory proposed that there is a relationship between the value of the firm and dividend yield. It stipulated that dividends are less risky than capital gains since they are more certain. Investors prefer to receive dividends 'today' than in future because current dividends are more certain than future capital gains that might be realized from investing retained earnings in growth opportunities (Gordon, 1962), and (Weston, 1963). Because of the uncertainty, investors prefer current dividends (even if they are lower) to future capital gains therefore, a bird in the hand (dividend) is worth more than two in the bush (capital gains).

Since the theory proposed that there exists a relationship between dividend yield and financial performance of the firm, it was of much relevance to this study which sought to prove if there is relationship between dividend yield and financial performance.

Empirical review regarding the study variable was conducted. Murimi and Mungai (2021) used dividend yield as one of the independent factors impacting the financial performance to examine the impacts of dividend policy on the financial performance of insurance businesses listed in Nairobi Securities Exchange, Kenya. From their findings it was revealed that dividend yield has a positive effect on the performance of insurance companies listed at the Nairobi Securities Exchange. The study therefore used the same variable for the entire firms listed at NSE to come up with a conclusion which applies to all firms at NSE, Kenya.

Osakwe et al. (2019) examined the effect of dividend policy on stock prices with empirical evidence from Nigeria. Their study applied dividend yield dividend yield as one of the independent variables measuring dividend policy. The results showed that dividend yield had an insignificant negative effect on market price per share. The study used the same independent variable dividend yield to investigate the relationships between dividend pay-out and financial performance of all firms listed at the Nairobi Securities Exchange.

Kanakriyah (2020) conducted a study to examine the nature of the correlation between dividend policy and a corporation's financial performance in developing countries. The results detected a strong relation between dividend yield and firm performance. Since the study was conducted out of the scope of Africa, it might not be applicable in Kenya and that's the reason why the researcher conducted the same study in the Kenyan context.

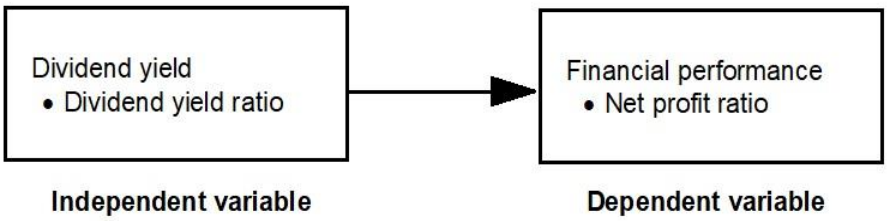
Memon et al. (2017) in their study examined the effect of dividend policy on market prices of firms' stocks of the nonfinancial sectors of Pakistan during the period from 2006 to 2015 which their findings revealed that there is a negative significant impact of dividend yield on stocks market prices. This study therefore intends to use firms from all sectors, in order for all firms at NSE, Kenya to benefit from its findings.

Kim (2020) assessed the link between Korean stock returns, dividend yield, and dividend reputation. Findings showed that dividend yield depends on a firm's dividend reputation. The data revealed that corporations with higher yields that have a reputation for paying

dividends generate greater future returns, but firms with no reputation had no discernible association between yields and returns. The study was excellent overall, although it was conducted in an advanced Asian nation. Thus, by focusing on an African emerging nation, the study addressed a vacuum in the geographic literature.

Figure 1

Conceptual framework



Dividend yield is the financial ratio that measures the amount of cash dividends paid out to shareholders relative to the market value per share. The study operationalized this variable by finding the dividend yield ratio which measures the return on investment in share and it's calculated by dividing dividend per share with the stock price.

Profitability is a measure of the organizations profits relative to its expenses. The study used net-profit ratio which is a ratio that measures the relationship between net profits and net sales, it done by dividing net profit with net sale.

3. Research Methodology

An explanatory research design was adopted by the study which was conducted in Kenya with the main focus was only firms listed at NSE. All the 62 firms listed in the Nairobi Securities Exchange for the period between 2018 to 2020 were considered in the study. Secondary data from the firm's published financial statements were collected by use of a data collection sheet. Collected data was analysed using descriptive statistics. Simple linear regression was carried out in testing the relationship between dividend yields and financial performance as illustrated in the equation (1), below.

$$Y = \alpha + \beta_1 D_Y + \varepsilon \quad (1)$$

Where Y is financial performance, D_Y is the dividend yield, α is the constant term, β_1 is the coefficient used to measure the sensitivity of the dependent variable a unit change in the predictor variable and ε is the error term used to capture unexplained variations in the model and which is assumed to be normally distributed with a mean of zero and a constant variance.

4. Results and discussions

All the 62 companies listed on the NSE have participated in the study. All the financial records were accessed from these firms during the study period. This represents a 100% response rate.

The financial performance of the listed firms in NSE were assessed using the net profit ratio, and the results are as shown in Table 1.

Table 1

Financial Performance of the Listed Firms

Year	Mean	Standard deviation	Min	Max
2018	0.257381	0.531611	-0.4782	2.4266
2019	0.145513	0.597094	-2.7595	2.218
2020	0.107766	0.5329	-1.6835	2.165
Aggregate mean performance	0.17022	0.55537	-2.7595	2.4266

Source: author's calculation

The descriptive results above show that in 2018 the aggregate financial performance of the listed firms was 0.257381, declining to 0.145513 in 2019 and further declining to 0.107766 in 2020 an indication that profitability of listed firms has been declining from 2018 to 2020. The standard deviation was 0.531611in 2018, 0.597094 in 2019 and 0.5329 in 2020 an indication that the average financial performance across the listed firms was clustered around the mean response. The results of net profitability ratio show that the net profitability ratio had a mean of 0.17022 and a standard deviation of 0.55537. The standard deviation of 0.55537 implies that the net profitability ratio varied over time during the study period. Profitability is a measure of the organizations profits relative to its expenses. Financial performance measures the outcome of the organization's strategies, policies, and operations in terms of money.

The descriptive statistics for dividend yield includes the mean, standard deviation, minimum and maximum values. These results are presented in Table 2.

Table 2

Dividend Yield among the Listed Firms

Year	Mean	Standard deviation	Min	Max
2018	0.307596	0.324342	0.000	1.38
2019	0.287107	0.335429	0.000	1.491
2020	0.234056	0.321101	0.000	1.572
Aggregate Dividend Yield Ratio	0.276253	0.326724	0.000	1.573

Source: author's calculation

According to data presented in Table 2, in 2018, the aggregate dividend yield ratio for the listed firms was 0.307596, declining to 0.287107 in 2019 and further dropping to 0.234056 in 2020. The standard deviation was0.324342 in 2018, 0.335429 in 2019 and 0.321101 in 2020 an indication that the average dividend yield ratio across the listed firms was clustered around the mean response. The overall mean of dividend yield ratio is 0.27625 and the standard deviation is 0.32672. The standard deviation of 0.32672 indicate that the dividend yield ratio changed over time during the study period.

Regression results

OLS regression was conducted to determine the relationship between dividend yield and the performance of listed firms measured by profitability.

Table 3

Model Summary of Dividend Yield

Model Summary	2018	2019	2020
R	0.375	0.421	0.628
R Square	0.141	0.177	0.394
Adjusted R Square	0.127	0.163	0.384
Std. Error of the Estimate	0.496846	0.546211	0.418236

Source: author's calculation

Model summary in Table 3 showed that in 2018, dividend yield explained 14.1% of the financial performance oft listed firms at NSE, 17.7% in 2019 and 39.4% in 2020.This is an indication that dividend yield overtime from 2018 to 2020 has been adopted by listed firms to enhance performance of listed firms at NSE. The R-square for regression models using secondary data are generally low. The low R-squared is an indication of high-variability data which still can depict significant trend.

Table 4 shows the ANOVA results for 2018-2020, indicating whether the overall model is statistically significant.

Table 4

ANOVA Results of Dividend Yield and Financial Performance Listed Firms

	Model	Sum of Squares	Df	Mean Square	F	Sig.
2018	Regression	2.428	1	2.428	9.835	.003
	Residual	14.811	60	.247		
	Total	17.239	61			
2019	Regression	3.847	1	3.847	12.894	.001
	Residual	17.901	60	.298		
	Total	21.748	61			
2020	Regression	6.828	1	6.828	39.033	.000
	Residual	10.495	60	.175		
	Total	17.323	61			

Source: author's calculation

As displayed in Table 4, the ANOVA model results in 2018 was statistically significant, an indication that dividend yield is a satisfactory indicator of performance of listed firms (F statistic of 9.835; p value =.003<0.05). Similarly, the dividend yield in 2019 (F statistic of 12.894; p value =.001<0.05) and 2020 (F statistic of 39.033; p value =.000<0.05) were statistically significant across time period in financial performance of firms listed at NSE. The ANOVA results supports the hypothesis that dividend yield has a positive and significant effect on the performance of the listed firms at NSE.

Table 5 shows the model coefficient results.

Table 5

Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
2018	(Constant)	.068	.087		.781	.438
	Dividend Yield Ratio	.615	.196	.375	3.136	.003
2019	(Constant)	-.069	.092		-.758	.452
	Dividend Yield Ratio	.749	.208	.421	3.591	.001
2020	(Constant)	-.136	.066		-2.065	.043
	Dividend Yield Ratio	1.042	.167	.628	6.248	.000

Source: author's calculation

It was established that dividend yield in 2018 was statistically significant with performance of listed firms at NSE (β=.615, p-value=.003<0.05). Likewise, dividend yield in 2019 (β=.749, p-value=.001<0.05) and 2020 (β=1.042, p-value=.000<0.05) had statistically significant relationship with performance of listed firms at Nairobi Securities Exchange. The beta coefficients have been increasing overtime from .615 in 2018 to .749 in 2019 and 1.042 in 2020 which indicate that dividend yield has been increasing becoming important in stimulating performance of the listed firms in NSE over time. The results were in agreement with research conducted by Murimi and Mungai (2021) on the dividend policy effects on financial performance of insurance companies listed in the Nairobi securities exchange and found out that dividend yield has a positive effect on the performance of insurance companies listed at the Nairobi Securities Exchange.

The regression results indicated that dividend yield is positive and significantly related with the performance of the listed firms in NSE (β=0.3728, P=0.006<0.05). This means that a unit increase in the dividend yield leads to .3728 units increase in the performance of the listed firms in NSE. The null hypothesis that there is a no significant relationship between dividend yield and financial performance amongst listed firms at NSE was therefore rejected. Increased dividend distributions improve the financial performance of NSE listed companies.

5. Conclusion and recommendations

The study concluded that dividend yield has a positive and statistically significant relationship with the financial performance of the firms listed at NSE.

The study recommends that the listed firms should strive to have a sizable amount of the profits accrued by the firm be paid as dividends. This will boost the confidence of the shareholders and will be able to make more investments in the firm. As a result, the financial performance of the listed firms will be boosted, hence generating more and more investments.

The study found out after the analysis of the study data that even though the variable selected in the study was able to explain the variations in the financial performance of the listed firms, the study recommends that further research be conducted on the effect of nature of ownership and the financial performance of the listed firms at NSE.

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