DIVIDEND POLICY AND FIRM MARKET VALUE IN NIGERIA: A PANEL DATA STUDY

UGORJI-EKE, PATIENCE NNENNA
Lecturer, Department of Banking and Finance
Abia State Polytechnic, Aba

URUAKPA, NAPOLEON IREOKWU
Lecturer, Department of Banking and Finance
Abia State Polytechnic, Aba

And

KALU, UGO EKE
Lecturer, Department of Banking and Finance
Abia State Polytechnic, Aba.

Abstract

This study considers empirically the relationship between dividend decisions and the market value of 9 quoted companies in Nigeria using the three conventional panel data models; pooled OLS, fixed effects and random effects. The companies are Academy press, BOC Gases, First Bank of Nigeria, Guinness, Julius Berger, Lafarge, Nigerian Breweries, Nestle and United Bank of Africa. The study covers a period of 6 years from 2010 to 2015. Consistent with the signaling theory of dividend, our results suggest that dividend payments have positive influence on the firm market value. A 1% increase in dividend per share would lead to approximately 0.16% increase in the firm market value. Also, consistent with the fixed effects theory, the firm-specific effects have significant explanatory power for firm market value and are correlated with dividend policy variables.
Key words: Dividend policy, firm market value, fixed effects.

Introduction

The concern of dividend policy is a very significant one in the current business environment. Dividend policy remains one of the essential financial policies not only from the perspective of the firm but also from that of the shareholders, the consumers, employees, regulatory bodies and the Government. Hence For a company, it is a central policy in which other financial policies revolve (Alii et al., 1993). Besides, dividend policy decision is acknowledged as one the most controversial parts of financial management. It has been further established by Baker and Powell (2000) as one of the most important financial decisions that corporate managers encounter. Despite the several studies done in this area, a consensus is yet to be reached. Kalay, Lowenstein and Sarig (2000) described dividend policy as the practice that management follows in making dividend payout decision.

Furthermore, Dividend policy aids as a mechanism for control of a managerial opportunism. Empirical studies show that organizations in developing countries (e.g. Nigeria) smooth on their income and therefore, their dividends. The pattern of corporate dividend policies not only varies over time but also across countries, especially between developed, developing and emerging capital markets. If the value of a company is the function of its

dividend payments, dividend policy will affect the organization cost of capital directly. Hence dividend allocation decision is one of the four decision areas in finance. Dividend policy is crucial because it determines what funds flow to investors and what funds are retained by the companies for reinvestment (Ross, Westerfield & Jaffe, 2002). Therefore, they provide information to stakeholders concerning the firm's performance. The investments of firms determine future earnings and future potential dividends and also influence the cost of capital (Foong, Zakaria & Tan, 2007).

The research work of Miller and Modigliani (1961) lays the foundation for the study of dividend policy in the modern era. They claim that in certain perfect market conditions, dividend policy is irrelevant. Hence, researchers have made efforts to build literature by considering situations where one or two of the ideal conditions as emphasized in the Miller and Modigliani irrelevant hypothesis are relaxed. Results of these studies are varied, although most of them conducted in developed countries.

Here in Nigeria, the survival of any firm is dependent on the continuous investment in facilities and the service of internal financing, via the usage of retained earnings through an essential part of the sources of finance to pay the investment needs (Bajaj & Vijh 1990; Osaze & Anao, 1990). The fiscal policies of government tend to put some restrictions on the amount of dividend a firm may pay. This has formed part of the realized profits to be ploughed back. This was very evident during the indigenization exercise of the seventies. The restriction reinforced by section 379 (2) of the company and allied matters act (CAMA) 1990, which then provides that the general meeting shall have the power to decrease the amount recommended. The dividend decision policy in Nigerian is to ensure that funds are available for constant investment in assets so that the firms will continue to operate on the going concern principle. Lack of sufficient funds has subdued the actualization of laudable goals of an entrepreneurial venture in Nigeria. Furthermore, the low level of investment capital accessible to most industrial organizations has accounted for the low capacity utilization.

Furthermore, the Manufacturers Association of Nigeria recently put this at below 30% (NigeriabusinessInfo.com). As one of the reactions to the agony of capital shortage in the industrial sector, the Nigerian government introduced the deregulation of the capital market. The excess was to nurture a developed capital market. However, irrespective of the numerous laudable efforts by the government, the Nigerian capital market is still in its emerging state. Hence, in the face of this looming shortage predicament.

This present research adds to the existing literature by examining the relationship between dividend policy and firms' financial performance in Nigeria, in an emerging economy studies conducted in developing countries (Nigeria) so far are very limited, hence the need for this study.

The other sections of the paper are organized as follows: Section 2 presents the literature review, which also incorporates the related empirical studies from other climes, particularly the developing countries. Section 3 deliberates on the methodology of the study. Results and discussion of the research are presented in section 4 while section 5 concludes the study.

Literature Review
Theoretical framework

Dividend policy is analyzed as one of the most controversial issues in corporate finance literature and still plays a significant role both in developed and emerging markets (Hafeez & Attiya, 2009). Many researchers have strained to uncover issues regarding the dividend dynamics and determinants of dividend policy but there is not an acceptable explanation for the observed dividend behaviour of firms (Black, 1976; Brealey & Myers, 2005). Hence, Since the research work of Miller and Modigliani irrelevant hypothesis, various theories have been developed by researchers to explain dividend policy decision.

MM Irrelevance theory

Modigliani and Miller in their 1961 research suggested that under certain assumptions about a perfect capital market, dividend policy decisions being implemented by a firm will not affect its rate of returns and market value. They also argued that despite how the firm distributes its income, the market value of the organization would not be affected because its value is determined by its primary earning power and its investment decision. Besides, this point has been fundamentally criticized by several authors because in real life situations we have imperfect market conditions such as transaction cost, agency cost taxes and asymmetric information (Allen & Michaely, 2002; Amidu & Abor, 2006; Fama & French, 2002; Gordon, 1961, 1962; Lease, John, Kalay, Lowenstein, & Sarig, 2000). Furthermore, Dividend policy has been analysed for many decades, but it has not yet achieved a widely accepted explanation for companies' observed dividend behaviour has been established (Samuel & Edward, 2011). It is said to be a long puzzle in corporate finance. Miller and Modigliani (1961) are of the opinion that under certain simplifying assumptions, the dividend decision does not impact the value of a firm and is, hence, unimportant. Traditional wisdom with changed assumptions advocates that a properly managed dividend policy is vital to shareholders because it can impact share prices and shareholder's wealth. Therefore, this argument is achieved on two assumptions; firstly, that there is no disadvantage to an investor to receiving dividends, secondly firms can raise funds in capital markets for new investments without bearing any significant issuance costs. In this line of thought, the proponents of the second think that dividends are disadvantageous to the average stockholder due to the tax disadvantage they create, which returns in a lower value. Lastly, there are those in a third group who argued that dividends are clearly good because stockholders like them. Hence, despite voluminous findings on bonuses, financial economics and corporate managers still face what Black (1976) once described as a dividend enigma with pieces of a puzzle that don't seem to fit.

Bird-in-hand Hypothesis

This hypothesis explains that increase dividend payout decisions affect firm value positively. The proponents of this hypothesis claim that due to the existence of market imperfections and uncertainty, dividends are always valued differently from capital gains. Hence, investors still prefer the "bird-in-hand" (cash dividends) to "two-in-the-bush" (future capital gains). Although many researchers have severally challenged this hypothesis, yet it has

received overwhelming support from research carried up by Lintner (1962), Walter (1963), Gordon (1963), Bhattacharya (1979), Miller and Rock (1985).

Tax Preference Hypothesis

This hypothesis projected that low-dividend payout ratios lower the rate of returns, which in turn ultimately increase the market value of the firm and vice versa. It claimed that the impact and treatment of taxes might have an effect on income to be distributed by a firm. In some countries, the rates in tax effect dividends are different from capital gains tax rate. Therefore, investors in different tax bracket will have a different opinion regarding whether to accept cash dividends or obtain capital gains (through the disposal of the securities). Consequently, according to the hypothesis, investors in high tax bracket are vulnerable to higher pre-tax risk and premium returns to hold stocks with higher dividend yield. Thus, Poterba and Summers (1984) and Kalay and Michaely (2000) provided analysis in support of the tax preference hypothesis.

Clientele Effects Theory

This theory proposed that investors/ clienteles are affected differently by dividend policy decisions adopted by firms. While most investors will prefer companies that pay a substantial amount of their earnings in the form of dividends, other groups of investors may prefer the ones that retained a greater proportion of their earnings. Both tax treatment of dividends and capital gains are considered as an essential aspect in investors having diverse behaviours toward dividends and capital gains. For instance, companies that pay a large number of their earnings as dividends will attract a client that prefers a high dividend, while those in the high-tax bracket will prefer companies that pay low dividends or no dividends and also favour capital gains. Therefore, provision for this concept involves the research of Dhaliwal, Errickson and Trezevant (1999), Allen, Bernado and Welch (2000), Seida (2001) and Short, Zhang and Keasey (2002).

The Agency Cost Hypothesis

In recent business activities, a principal-agency relationship exists between the company's shareholders (principal) and managers (agents). The managers are often expected to act always in the best interest of the shareholders. In most cases, however, the hypothesis suggested that managers tend to work in a way that is unfavourable to the benefit of the shareholders (for instance, by investing in negative NPV projects, by increasing their perquisites, etc.). The hypothesis recommends that dividend payments can be used to alleviate this agency costs in two ways. Firstly, by paying dividends, the company will also have the prospect of accessing additional funds from the capital market. Hence, this will make it possible for the new investors; stakeholders and general public analyze the financials of the firm, thus reducing the agency cost. Secondly, paying dividends will drastically reduce the amount of surplus fund available to managers which will not utilize in the best interest of the owners of the business (shareholders). Research spearheaded by Jensen (1986), Demsey and Laber (1992), Jensen, Solberg and Zern (1992), Gaver and Gaver (1993) and Al-Malkawi (2005) were in line with this hypothesis.

Signaling Hypothesis

This hypothesis specified that dividend announcements have valuable information, which is known as signals, relating to futuristic earnings of the firm. Thus, the rise in dividend payout, relating to this hypothesis, sends a positive signal to the investors and the public that the future earnings of the company are bright. More so, the reverse is the case for a company that drastically reduces its dividend payout or did not pay dividends. For the signal to be important, the hypothesis claims that the signal being sent by the firm through dividend announcements should be accurate. Thus, bad firms (with low-or-no dividend payout) should not be able to imitate a good firm (with high or increase payout) by declaring a high dividend. The cost of the imitation should be elevated to discourage the bad firm from passing a bad signal to the market. Besides, Pettit (1977), Asquith and Mullins (1983), Nissim and Ziv (2001), Travlos, Trigeorgis and Vafeas (2001) and Bali (2003) provided evidence consistent with the prediction of this hypothesis.

Related Empirical Studies

From empirical literature, the relationship between dividend payout ratio and performance is mixed. Most research suggests a positive relationship while others support a negative relationship. Few of such analyses also confirmed no ties. The debate on the directional effect on the relationship between the two variables continues. Hence, Oyejide (1978) found a statistically significant association between current year dividends and past year net profit in a study conducted in Nigeria in the 1970s. Baker et al. (2007) noticed that Canadian firms are paying dividends remarkably more significant with higher profits. Al-Kuwari (2009) recommended that profitability ratio is the critical determining factor of corporate dividend policy in listed firms of Gulf Co-operation Council countries, while Pandey (2001) identified and analyzed it on Malaysian firms. Afzal and Mirza (2010) find a positive association of operating cash flow and profitability with dividend policy.

Kale and Noe (1990) are of the opinion that a firm's dividend indicates the stability of the firm' future cash flows. A review from previous studies emphasized that the main factors that influence a firm's dividend decisions include cash flow considerations, liquidity, and future earnings investment returns, after-tax earnings, past dividend practices, inflation, interest, legal requirements and the future growth projection. Their view, however, supports the suggestions of Brigham (1995) where a firm's dividend policy describes as a major determining factor for a firms' performance. Thus, Zakaria and Tan (2007) also stressed the same line of thought that investments made by firms' influences future earnings and future dividends potential.

Zeckhauser & Pound (1990) are of the opinion that there is no significant difference among dividend payouts with or without large block shareholders. Besides, Kouki and Guizani (2009), and Kumar (2006) also added in their research that managerial ownership appears to have a visible and significant impact on dividend payout.

Uwuigbe, Jafaru and Ajayi (2012) scrutinized the relationship between the financial performance and dividend payout among 50 listed firms in Nigeria for 2006 to 2010. The result shows an essential and positive association between the performance of firms and the dividend payout. The research also reveals that ownership structure and firm's size has a significant impact on dividend pay-out of firms.

Oyinlola and Ajeigbe (2013) studied the impact of dividend policy on the stock prices of 22 quoted companies in Nigeria during the period 2009 to 2013. Regression analysis, correlation analysis and Granger Causality Test were used to test the research hypothesis on 110 observations. Findings reveal that both dividend payout and retained earnings are significantly relevant to the market per share of the companies.

Ouma and Murekefu (2013) sought to establish the relationship between dividend payout policy and financial performance of various firms listed on the Nairobi Stock Exchange. Results indicate that dividend payout is a significant factor affecting firm performance. The relationship between both variables is positive and significant.

In conclusion, while numerous prior empirical studies from developed economies have carried out a comparative analysis between dividend payout and firm performance, the same is not true in emerging economies like Nigeria. Therefore, this study, thus, tends to fill this gap in the literature by examining the relationship between the financial performance of firms and the dividend payout of listed firms in Nigeria. The research will, also, attempt to find whether there is a relationship between firm size, dividend payout and ownership structure in listed firms in Nigeria.

Research Methodology
Data

This study uses a panel data to investigate the impact of dividend policy on firm's performance in Nigeria. The panel consists of 9 publicly quoted companies from the consumer goods sector in Nigeria observed for 6 years from 2010 to 2015. However, the panel is unbalanced as there are some missing date observations within the dataset. The companies are Academy press, BOC Gases, First Bank of Nigeria, Guinness, Julius Berger, Lafarge, Nigerian Breweries, Nestle and United Bank of Africa. The data are all collected from the annual reports and accounts of the selected companies and are analyzed in E-Views.

Methods and Models

In this study, three panel estimation approaches are used; pooled regression, fixed effects and random effects approaches. The motivation for using these methods is to capture the effects of firm-specific differences that may be significantly influencing the dependent variables.

The Pooled Regression Model can be Specified as:

$$MVS_{it} = \alpha + \beta_1 DPS_{it} + \beta_2 RPS_{it} + \beta_3 TAX_{it} + \beta_4 ASSET_{it} + \epsilon_{it} \tag{1}$$

Where MVS_{it} is the market value per share which proxies the firm market value, DPS_{it} is dividend per share; RPS_{it} is retained earnings per share; TAX_{it} is the taxation, $ASSET_{it}$ is total asset and ϵ_{it} are error disturbances that follow the classical regression assumptions. The subscripts i represents $1, 2, …, N$ cross-sessional units while subscript t represents $1, 2, …, T$ time periods. While α is the intercept, β is the beta coefficient that capture the effect of non-current asset on market value per share. The pooled model assumes that firm-specific effects are not significantly related with market value per share; hence, the intercept has no subscript i.

The Fixed Effects Model can be Specified as:

$$MVS_{it} = \alpha + s_i + \beta_1 DPS_{it} + \beta_2 RPS_{it} + \beta_3 TAX_{it} + \beta_4 ASSET_{it} + \epsilon_{it} \tag{2}$$

Where: $MVS_{it}, \alpha, \beta, NCL_{it}, CL, TE$ and ϵ_{it} are as defined in (1), s_i is the unobserved fixed effects which capture the cross-sectional heterogeneity in the panel data. The subscript attached to s_i indicates that $s_1, s_2, \dots, s_N$ vary cross-sectionally but remain constant overtime. The fixed effects model also assumes that the fixed effects model assumes that each s_i is a significant determinant of each MVS_{it} and correlates with DPS_{it}, RPS_{it}, TAX_{it}, and $ASSET_{it}$. Thus, s_i is the difference between model (1) and model (2).

The Random Effects Model can be Specified as:

$$MVS_{it} = \alpha + \beta_1 DPS_{it} + \beta_2 RPS_{it} + \beta_3 TAX_{it} + \beta_4 ASSET_{it} + s_i + u_{it} \tag{3}$$

Where: α is the overall mean, r_i is a random deviation from this mean and u_{it} is the error term. Since both s_i and u_{it} are random deviations, the random effects model merges the two errors to form the composite error term, with the assumption that s_i is uncorrelated with $NCL_{it}, CL_{it}, and\ TE_{it}$ The random effects model with composite error term is thus given by:

$$MVS_{it} = \alpha + \beta_1 DPS_{it} + \beta_2 RPS_{it} + \beta_3 TAX_{it} + \beta_4 ASSET_{it} + w_{it} \tag{4}$$

where; $w_{it} = s_i + u_{it}$ is the composite error term. Compared with the pooled OLS model, both fixed effects and random effects models recognize the effect of the firm-specific factors that are not directly observed by including a specific parameter for these factors. However, the difference between these models lies in whether s_i is correlated with DPS_{it}, RPS_{it}, TAX_{it}, and $ASSET_{it}$ or not. Both Likelihood ratio and Hausman specification tests are available to test which of these models makes the right assumption for our panel data.

Data Analysis and Discussion

In table 1, the estimation results for pooled regression model, fixed effects model and random effects model are reported. We can see that coefficients on LDPS is consistently positive and significant, although the significance is weak for fixed effects model (p-value = 0.0918). Thus, consistent with signaling hypothesis, dividend payment is associated with increase in the firm's value. Both LRPS and LTAX all are also consistently associated with positive coefficients, suggesting that retained profit and corporate tax also have positive relationship with firm market value. However, while the effect of retain profit is only significant for the pooled model, the effect of corporate tax is significant for both the pooled regression and random effects model but insignificant for the fixed effects model. The coefficient on LTASSETS is not significant for all models, although, its sign varies.

In terms of goodness of fit, the results suggest that the fixed effects model performs better than both the pooled model and random effects model. The fixed effects adjusted R-squared is quite high at 0.9581 compared to that of the pooled regression model and the random effects model which is 0.8382 and 0.4455 respectively. However, the F-statistic is highly significant for all models, suggesting that the market value model is well explained.

Variable	Pooled OLS	Fixed Effects	Fixed Effects
Constant	1.8610 (0.0159)	1.2913 (0.7781)	4.2508 (00007)
LDPS	0.3183 (0.0004)	0.1605 (0.0918)	0.3309 (0.0000)
LRPS	0.3312 (0.0022)	0.0145 (0.8342)	0.0792 (0.2402)
LTAX	0.3362 (0.0022)	0.1018 (0.2748)	0.1817 (0.0259)
LTASSET	-0.0694 (0.1725)	0.2411 (0.2687)	-0.0228 (0.6546)
R-square	0.8523	0.9690	0.4937
Adjusted R-square	0.8382	0.9581	0.4455
F-statistic	60.5857 (0.0000)	88.5471 (0.0000)	10.2395 (0.0000)

Table 1: Estimation Results for Pooled, Fixed Effects and Random Effects Models

The firm-specific characteristics models are reported in table 2. The table shows that firm-specific effects have similar effects for all companies, except for UBA. While Academy Press, Boc Gases, First Bank of Nigeria, and Julius Berger having negative individual-specific effects, Guinness, Lafarge, Nigerian Breweries and Nestle all have positive firm-specific effects.

Table 3 shows the likelihood ratio test for comparing pooled model estimates with those of the fixed effects, and table 4 shows the Hausman test for comparing the results of the random effects with those of the fixed effects. These tests are used to test whether the firm specific effects are relevant, and if yes, whether they are correlated with the observed explanatory variables. While the likelihood ratio test is conducted under the null hypothesis of irrelevant fixed effects, the Hausman test is conducted under the null hypothesis that these fixed effects are uncorrelated with DPS, RPS, TAX and TASSETS.

S/no	Company	FEM	REM
1	Academy	-0.5871	-0.8935
2	BOC Gases	-0.1332	-0.7859
3	First Bank of Nigeria	-3.3785	-0.9105
4	Guinness	1.5067	0.7352
5	Julius Berger	-0.0547	-0.3002
6	Lafarge	0.5556	0.2326
7	Nigerian Breweries	0.7957	0.2900
8	Nestle	2.5667	1.4413
9	UBA	-2.9975	0.1910

Table 2: Estimated Firm-Specific Effects

Effects Test	Statistic	d.f.	p-value
Cross-section F	15.9966	(8,34)	0.0000
Cross-section Chi-square	73.3701	8	0.0000

Table 3: Likelihood Ratio Test for Estimated Fixed Effects

Test summary	Chi-Square Statistic	d.f.	p-value
Cross-section random	18.6375	4	0.0009

Table 4: Hausman Test for Correlated Random Effects.

From table 3, the two variants of the likelihood ratio test are highly significant, suggesting that firm-specific effects are relevant. From table 4, we can see also that the Hausman test is highly significant. We therefore strongly reject the assumption that-firm specific effects play insignificant role in the market value model, and the assumption that they are uncorrelated with the observed factors in the model. In other words, fixed effects model outperforms its competitors.

Conclusion

This study considers empirically the relationship between dividend decisions and the market value of 9 quoted companies in Nigeria using the three conventional panel data models; pooled OLS, fixed effects and random effects. The companies are Academy press, BOC Gases, First Bank of Nigeria, Guinness, Julius Berger, Lafarge, Nigerian Breweries, Nestle and United Bank of Africa. The study covers a period of 6 years from 2010 to 2015.

Our main conclusion is that although, dividend payments provide signalling information to investors in the stock market, its effect on the firm market value is weakly significant. A 1% increase in dividend per share would lead to approximately 0.16% increase in the firm market value. We also concluded that the firm-specific effects are significant determinants of market

value of quoted companies and are correlated with their dividend policy variables. Our results contradict the popular Modigliani and Miller (1961) but agree with most of the empirical studies both in developing and developed countries.

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