

Determinants of Dividend payout: An Empirical Study in Ethiopian Private Banks

Elias Mitiku

Abstract

The main purpose of the study was to examine the determinants of dividend payout in Ethiopian private banks. Five years data from 2009/10 to 2013/14 were collected from National bank of Ethiopia and banks audited financial statement. The collected data were analyzed using panel data regression technique. The study used dividend payout as a dependent variable and seven independent variables; they are profitability, liquidity, leverage, lagged dividend payout, growth, size and risk. The finding indicated that among the seven independent variables; lagged dividend payout, growth, size and risk have statistically significant impact on dividend payout; the rest three variables have no statistical significant impact on dividend payout. Therefore, lagged dividend payout, growth, size and risk have a significant impact on dividend payout in Ethiopian private banks and board of directors of banks need to consider these variables while designing their dividend payout policy; on the same token investors need to consider these variables in their investment decisions when they want to make an investment in Ethiopian private banks.

Keywords: Dividend payout, Private Banks

1. Introduction

Dividend policy is one of the most controversial issues in modern corporate finance (Maladjian & El Khoury, 2014). Explaining why companies pay dividend and some do not pay dividends is still problematic to explain and therefore, dividend policy remains controversial (Ross, Westerfield, & Jaffe, 2002; Brealey & Myers, 2003; Badu, 2013). The debate around the importance of dividend payment by corporations as a value adding activity is still unresolved because of some advantage and disadvantage attached to it. Many reasons exist why companies should pay or not pay dividends. Yet figuring out why companies pay dividends and investors pay attention to dividend that is the “dividend puzzle” is still problematic (Ross et.al, 2002). Dividend policy is defined as the payout policy that managers follow in deciding the size and pattern of cash distribution to shareholders (Sheikh Taher, 2012). Different theories have developed to describe dividend payout policy and its factors such as theory of agency, dividend irrelevance theory, pecking order theory, signaling theory, bird-in-the-hand theory and tax preference theory. As per the model of Miller & Modigliani (1961) dividend policy is irrelevant under perfect capital market because it has no effect on either the price of firm’s stock or its cost of capital. The presence of market imperfections, such as taxes, asymmetric information, agency costs, and transaction costs means, that we cannot dismiss the proposition that dividend policy is relevant to the firm’s value (Al-Shubiri, 2011).

Several empirical studies have been conducted to identify major factors that affect the dividend payout policy of companies (Amidu & Abor, 2006; Sheikh Taher, 2012; Badu, 2013; Maladjian & El Khoury, 2014). For instance, Lintner (1956) indicated that the dividend payment pattern of a firm is influenced by the current year’s profit and previous year’s dividend payment; managers prefer stable dividend payout policy. Badu (2013) studied the determinants of dividend payout policy of

listed financial institutions in Ghana from 2005 to 2009 and has found statistically significant and positive relationship between age and liquidity with dividend payout but saw statistically insignificant relationship between profitability and collateral with dividend payout.

Maladjian & El Khoury (2014) studied the Lebanese banks to identify the factors that determines the dividend payout policy from year 2005 to 2011 and found that dividend payout policy is positively affected by the firm size, risk and previous year's dividends, but is negatively affected by the growth opportunity and profitability.

2. Statement of the problem

Different studies have been conducted on the dividend payout policy of companies for several years, different theories have been formulated and tested empirically, yet generalization becomes difficult on the factors believed to have significant impact on dividend payout policies (Brealey & Myers , 2003; Mehta, Hashmi, & Irshad, 2014). Among the prominent theories presented by Modigliani and Miller (1961) says under perfect capital markets without any taxes, transaction costs and other market imperfections, the company value is independent of the dividend policy. Instead the firm value is solely dependent on the earning power of the company's assets and its investment policy and not by how its profits are distributed to shareholders. Therefore, dividend is irrelevant. Against the dividend irrelevance theory by M&M other theories have claimed that dividend has relevance to companies.

Lintner's (1956) studies concluded that dividends are determined by a target payout level which depends on the company's long term earnings. Lintner's research was supported by Gordon (1959) who stated that shareholders prefer dividends rather than capital gains. If this is true, the company's dividend payouts are of major importance both to shareholders and managers, since it contributes to a higher value and shareholders would be willing to pay a higher price for stocks that pay dividends (Gustav & Gairatjon, 2012). The agency theory describes conflict of interest faces by managers between self-interest and shareholders interest. Hence managers may conduct actions according to their own self-interest at the cost of shareholders (Al-Shubiri, 2011). Dividend plays a crucial role in this agency problem resulting from excess free cash flow. When there is excess free cash flow, the management interested in external growth of the firm may undertake excessive investment and detrimental business expansion that can eventually cause the decrease of firm value and its share price (Lee, 2014). These and other theories have claimed, dividend is relevant.

Various studies have been conducted in order to determine the company factors that influence the dividend payouts. According to Lintner (1956) profitability and previously paid dividend has an impact on dividend payout policy of companies. Companies that are more profitable are expected to pay more dividends compared to those that are less profitable. This finding is similar to the finding of Maladjian & El Khoury, (2014); Kashif, (2011) and Lee (2014).

Even though, several empirical studies have been conducted on the determinants of dividend payout, the findings show differences. Although profitability is claimed to

have a positive impact on dividend payment by Lintner (1956) and Gordon (1959) and others, but the finding in developing countries shows profitability is not significant (Zaman, 2013; Nyor & Adekunle, 2013) or is negatively related with dividend payment (Maladjian & El Khoury, 2014). In spite of the continuous and increasing theoretical and empirical debate on dividend policy, there is still no generally accepted standard on how firms actually pay out dividend to shareholders at a given time period (Bassey, Elizabeth, & Asinya, 2014). In addition, almost all of the studies on this topic have been conducted on the countries where there are established stock markets used as a means to convert stocks held by shareholders into cash and only few studies have been conducted in the area of dividend payout in Ethiopian companies. Dagnaw (2009) and Kifle (2011) conducted a study to examine the determinants of dividend payout in Ethiopian private banks while Nuredin (2012) conducted the same study on Ethiopian Insurance companies.

Previous studies on determinants of dividend payout or policy were focused on developed countries where their corporate characteristics are different from developing countries (Badu, 2013). Differences in culture, corporate governance, tax, information asymmetry, and investors' attitude, and ownership structure are mentioned by Ahmed & Javid (2008) and Al-Malkawi (2008).

Only few studies have been conducted on the determinants of dividend payout in Ethiopia and they are not even recent. This shows that the research conducted in this topic is very limited in Ethiopia, where lots of share companies are emerging adjacently with the economic growth which demand public investment in these share companies and distribution of profit as dividend as a return for investment to shareholders. This condition requires more study to be conducted on the factors that determine dividend payout in Ethiopian private banks.

As stated by Sheikh Taher (2012) findings from several empirical studies suggest that risk along with published earnings, agency cost, size, taxes have more influence than others to determine the dividend payout of firms. The above stated three studies conducted in Ethiopian firms have not incorporated risk as a variable in identifying factors that determine dividend payout. Therefore, this study has incorporated the risk variable plus Ethiopia has no secondary markets for stock trade while previous studies conducted on the topic of determinants of dividend payout were focused only in those countries who have an established secondary market. Therefore, this study has conducted a research on the determinants of the dividend payout in Ethiopian private banks, where there are no secondary markets that could help investors to convert their stock easily into cash; and where there is a lack of enough and recent studies in Ethiopian companies.

3. Objective of the study

3.1 General objective

- The general objective of this study was to examine the determinants of dividend payout in Ethiopian private banks.

3.2 Specific objectives:

- To examine the impact of profit on the dividend payout of Ethiopian private banks.
- To determine the impact of liquidity on the dividend payout of Ethiopian private banks.
- To investigate the impact of leverage on the dividend payout of Ethiopian private banks.
- To explore the impact of firm size on the dividend payout of Ethiopian private banks.
- To identify the impact of growth on the dividend payout of Ethiopian private banks.
- To evaluate the impact of previous year's dividends on the dividend payout of Ethiopian private banks.
- To examine the impact of risk, earning volatility, on the dividend payout of Ethiopian private banks.

4. Hypotheses of the study

After reviewing the theoretical and empirical studies that covered determinants of dividend payout, this study has identified and formed the following eight alternative hypotheses:

Hypotheses 1: Profit has a positive relationship with dividend payout in Ethiopian Private Banks.

Hypotheses 2: Liquidity has a positive relationship with dividend payout in Ethiopian Private Banks.

Hypotheses 3: Leverage has a negative relationship with dividend payout in Ethiopian Private Banks.

Hypotheses 4: Previous year's dividends have a positive relationship with dividend Payout in Ethiopian Private Banks.

Hypotheses 5: Growth has a negative relationship with dividend payout in Ethiopian Private Banks.

Hypotheses 6: Firm size has a positive relationship with dividend payout in Ethiopian Private Banks.

Hypotheses 7: Risk has a negative relationship with dividend payout in Ethiopian Private Banks.

Hypotheses 8: Ethiopian private banks follow stable or smooth dividend policy.

5. Theoretical Framework

In discussing about dividend, it is important to highlight what a dividend is? Dividend is simply the money that a company pays out to its shareholders from the profits it has made (Ross et.al, 2002). Such payments can be made in cash or by issuing of additional shares as a dividend (Brealey & Myers , 2003). Investopedia, however defined it as the amount payable to shareholders from profit or distributable reserves; it is a distribution of a portion of a company's earnings, decided by the board of directors, to a class of its shareholders. Companies that are listed in the stock exchange are usually obligated to pay out dividends on a quarterly or semiannual basis. The semiannual or quarterly payment is referred to as the interim

dividend. The final payment, which is usually paid at the end of the financial year of the company, is known as the final dividend. Dividends are normally paid after the corporate tax has been deducted.

The decision whether or not to pay a dividend rests in the hands of board of directors of a corporation (Brealey & Myers, 2003). A dividend is distributable to shareholders of record on a specific date. When a dividend has been declared, it becomes a liability of the firm and cannot be easily rescinded by the corporation. The amount of the dividend is expressed as dollars per share (*dividend per share*), as a percentage of the market price (*dividend yield*), or as a percentage of earnings per share (*dividend payout*) (Corporate Finance, 2002; Ross et.al, 2002).

Dividend policies tend to be one of the most stable and predictable elements of a company, and most companies began to pay dividends once they reach a level of business maturity where attractive investment opportunities are generally less available while cash flow generation is stable or growing more slowly when compared to the past. Decreasing or eliminating a dividend is tantamount to an announcement that the firm is financially distressed. Directors weigh dividend policies very carefully, they rarely lower dividends unless they have to, and they do not raise dividends unless they are confident that it can be sustained (Ross et.al, 2002). When a company announces a larger than expected dividend or unexpectedly announces a dividend cut or omission, the market reaction is dramatic and sudden. Thus a stable dividend policy should convey stability or lower risk within the enterprise.

5.1 Theories of Dividend Policy

During the last fifty years several theoretical and empirical studies are done leading to the mainly two outcomes: the increase (decrease) in dividend payout affect the market value of the firm or the dividend policy of the firm does not affect the firm value at all (Ahmed & Javid, 2008). However, we can say that empirical evidences on the determinants of dividend policy are unfortunately very mixed. Furthermore there are numerous theories on why and when the firms pay dividends. Dividend policy has been the subject of considerable debate since Miller and Modigliani (1961) illustrated that under certain assumptions, dividends were irrelevant and had no influence on a firm's share price.

5.2 Dividend Irrelevance Theory

Prior to the publication of Miller and Modigliani's (1961) referred as M&M, seminal paper on dividend policy, a common belief was that higher dividends increase a firm's value. This belief was mainly based on the so-called "bird-in-the-hand" argument. However, as part of a new wave of finance in the 1960's, Miller and Modigliani demonstrated that under certain assumptions about perfect capital markets, dividend policy would be irrelevant (Al-Malkawi, Rafferty, & Pillai, 2010).

As the name of the theory suggests, it states that under perfect capital markets the dividend policy is independent to the value of a firm and it does not matter whether the company have high or low dividend payouts. They argued that the firm's value is determined only by its basic earning power and its business risk. In other words, M&M argued that the value of the firm depends only on the income produced by its assets, not on how this income is split between dividends and retained earnings

(Miller & Modigliani, 1961).

M&M also argue that the shareholders are able to construct their own homemade dividends. For example, if the company does not pay dividends but the shareholder prefers two percent dividend he can sell two percent of his stocks and thus create a homemade dividend. The opposite is of course also true, if the company pays a higher dividend than the shareholder prefers, he can use the surplus dividends to buy additional stocks. These two arguments discussed above are the underlying assumption of the irrelevance hypothesis and according to these arguments shareholders should be indifferent between capital gains and dividends. This in turn contributes to that the shareholders are unwilling to pay a higher price for dividend paying stocks which in turns make the question of dividends irrelevant(Corporate Finance, 2002;Ross et.al, 2002).

5.3 The “Bird-in the Hand” Theory

The name “bird in hand” is the umbrella term for all studies that argues that dividends are positively correlated to the company’s value. It is based on the expression that “a bird in the hand is worth more than two in the bush”. Expressed in financial terms, the theory says that investors are more willing to invest in stocks that pay current dividend rather than to invest in stocks that retain earnings and pay dividends in the future. This is due to the high degree of uncertainty related to capital gains and dividends paid in the future (Al-Malkawi et.al, 2010; Gustav & Gairatjon, 2012).

Gordon (1959) gave the bird in hand theory. He maintained that the discounted value of near future dividends is higher than the present value of distant dividends. He argued that the dividends to be received in future have much uncertainty as compared to the dividends in the near future since the shareholders would prefer certain returns the stock prices would be higher

5.4 Signaling Theory

Another hypothesis for why M&M’s dividend irrelevance theory is inadequate as an explanation of financial market practice is the existence of asymmetric information between insiders (managers and directors) and outsiders (shareholders). M&M assumed that managers and outside investors have free, equal and instantaneous access to the same information regarding a firm’s prospects and performance. But managers who look after the firm usually possess information about its current and future prospects that is not available to outsiders. This informational gap between insiders and outsiders may cause the true intrinsic value of the firm to be unavailable to the market. If so, share price may not always be an accurate measure of the firm’s value. In an attempt to close this gap, managers may need to share their knowledge with outsiders so they can more accurately understand the real value of the firm (Al-Malkawi et.al, 2010).

The signaling theory of dividends has its origins in Lintner’s (1956) studies who revealed that the price of a company’s stocks usually changes when the dividend payments changes. Even though M&M argued in favor of the dividend irrelevance they also stated that in the real world disregarding the perfect capital markets, dividend provides an “information content” which may affect the market price of the stock. Many researchers have thereafter been developing the signaling theory and

today it is seen as one of the most influential dividend theories (Gustav & Gairatjon, 2012). Signaling theory assumes that managers typically have more information about the value of the firm's assets than outside agents. Managers therefore use dividend changes to communicate to the shareholders about the financial situation of the company. The information may reflect the strategies that the firm is employing in the short run or long run (Ross, 1977).

5.5 Agency Theory

The agency theory is based on the principal agent relationships. The separation of ownership from management in modern corporations provides the context for the functioning of the agency theory. In modern corporations the shareholders (principals) are widely dispersed and they are not normally involved in the day to day operations and management of their companies rather they hire managers (agent) to manage the corporation on behalf of them (Habbash, 2010). The agents are appointed to manage the day to day operations of the corporation. The separation of ownership and controlling rights results in conflicts of interest between agent and principal. To solve this problem or to align the conflicting interests of managers and owners the company incurs controlling costs including incentives given for managers (ibid). This controlling cost is called agency cost (Easterbrook, 1984).

According to agency theory the agent strive to achieve his personal goals at the expense of the principal. Managers are mostly motivated by their own personal interests and benefits, and work to maximize their own personal benefit rather than considering shareholders' interests and maximizing shareholders wealth. To control and shape this inclination of managers, shareholders adopt monitoring schemes like payment of dividend. The costs of monitoring and bonding are agency costs borne by investors (ibid).

5.6 Tax Preference Theory

Taxation is one of the critical factors that affect firm value and future expected profits. For example, discounted expected after-tax cash flows can be used as a determinant for the market value of a firm. In this respect, differential tax treatment of capital gains relative to the dividends can influence the after-tax returns of investors and in turn affect the willingness of investors to receive dividends (Kinfe, 2011).

The tax-preference theory suggests that low dividend payout ratios lower the cost of capital and increase the stock price. In other words, low dividend payout ratios contribute to maximizing the firm's value. This argument is based on the assumption that dividends are taxed at higher rates than capital gains. In addition, dividends are taxed immediately, while taxes on capital gains are deferred until the stock is actually sold. These tax advantages of capital gains over dividends tend to predispose investors, who have favorable tax treatment on capital gains, to prefer companies that retain most of their earnings rather than pay them out as dividends, and are willing to pay a premium for low-payout companies. Therefore, a low dividend payout ratio will lower the cost of equity and increase the stock price earnings (Al-Malkawi et.al, 2010).

6. Research Methodology

The primary aim of this study was to examine the determinants of dividend payout in Ethiopian private banks. To achieve the objective explanatory type of research design with a quantitative approach method was employed.

Financial statement data were collected from National bank of Ethiopia and published audited annual reports of the banks included in the sample in order to examine the factors that affect the dividend payout of Ethiopian private banks. Five years data were collected from year 2009/10 up to 2013/14. A total of eight private banks were included in this study based on purposive sampling techniques. Because the below stated private banks are the only private banks that have started operation and distributed dividend on the study period from year 2009/10 to 2013/14. Panel data regression method is used to examine the relationship between dependent and independent variables in order to conclude based on the collected data about the determinants of dividend payout in Ethiopian private banks.

This study has two dividend models to test. The first model replicate Lintner's model in the Ethiopian private banks, the only variables included are profit and lagged dividend paid with dividend payout used as a dependent variable in order to determine whether Ethiopian private banks follow stable dividend payout policy or not. The second model is an extension of the first model by including additional independent variables in the model to examine the determinants of dividend payout in Ethiopian private banks. The data collected for the study has the dimension of both time series and cross sections. Therefore, balanced panel data regression technique is used in order to examine the determinants of dividend payout in Ethiopian private banks. To conduct the analysis, Eview 6 statistical software package has employed.

6.1 Model assumptions

The assumptions on classical linear regression model were tested to determine whether the collected data would fit the assumptions in order to use Ordinary Least Squares (OLS) technique. Consequently, the following basic CLRM assumptions were tested in this study:

Errors have zero mean, Heteroscedasticity, Autocorrelation, Multicollinearity, and normality. Finally, Hausman specification test is used to test the fixed effects model against the random effects model.

6.2 Model Specifications

Panel data involves the pooling of observations on a cross-section of units over several time periods and provides results that are simply not detectable in pure cross-sections or pure time-series studies. The panel regression equation differs from a regular time-series or cross-section regression by the double subscript attached to each variable. The general form of the panel data model can be specified more compactly as:

$$Y_{i,t} = \alpha_i + \beta x_{i,t} + \epsilon_{i,t}$$

With the subscript i , denoting the cross-sectional dimension and representing the time-series dimension.

In this equation,

$Y_{i,t}$ represents the dependent variable in the model, which is the firm's dividend payout ratio;

$X_{i,t}$ contains the set of explanatory variables in the estimation model; and

α_i is taken to be constant over time t and specific to the individual cross-sectional unit i .

In the light of the above model and on the bases of the selected variables, the current study used the below econometric model

$$\text{Model I: } DVPO_{i,t} = \alpha_i + \beta_1 \text{PRO}_{i,t} + \beta_2 \text{LDVP}_{i,t}$$

$$\text{Model II: } DVPO = f(\text{PRO}, \text{LIQ}, \text{LEV}, \text{LDVP}, \text{GRO}, \text{SIZ}, \text{RIS})$$

$$DVPO_{i,t} = \alpha_i + \beta_1 \text{PRO}_{i,t} + \beta_2 \text{LIQ}_{i,t} + \beta_3 \text{LEV}_{i,t} + \beta_4 \text{LDVP}_{i,t} + \beta_5 \text{GRO}_{i,t} + \beta_6 \text{SIZ}_{i,t} + \beta_7 \text{RIS}_{i,t} + \epsilon_{i,t}$$

Where,

DVPO= Dividend payout

PRO =Profitability

LIQ=Liquidity

LEV = Leverage

LDVP = lagged dividend paid

GRO= Growth

SIZ = size of the banks

RIS = Risk

Table.1 Variables Description and Expected Sign

Variable	Symbol	Description	Expected Sign
Dividend payout	DVPO	Dividend/net profit	Not Available
Profit	PRO	ROA= profit after tax and legal reserve/total asset	+
Liquidity	LIQ	Current asset/current liability	+
Leverage	LEV	Debt/Total asset	-
Lagged Dividend	LDVP	Last year dividend payout	+
Growth	GRO	(Current Revenue -Previous Revenue) /	-
Size	SIZ	Natural logarithm of total asset	+
Risk	RIS	Earning volatility- calculated by Log	-

6.3 Variables Construction

Based on previous researches on the determinants of dividend payout/policy, the following variables have been chosen in this study to be tested empirically, whether they have an impact on dividend payout of Ethiopian private banks or not. According to Creswell (2008), the variables need to be specified in quantitative researches so that it is clear to readers what groups are receiving the experimental treatment and what outcomes are being measured.

6.3.1 Dependent Variable

6.3.1.1 Dividend payout

Payout ratio is calculated by dividing the total dividend to net profit (Ross et.al, 2002). Most of the previous studies employed dividend payout ratios as a determinant of dividend in lieu of dividend per share and dividend yield (Amidu & Abor, 2006; Weber & Procyanoy, 2014; Maladjian & El Khoury, 2014). The dividend payout ratio is also used in this research, rather than dividend per share and dividend yield, for two reasons:

Firstly, the dividend payout ratio takes into consideration both dividend payout and dividend retention.

Secondly, dividend per share and dividend yield was considered unsuitable, because neither takes into account the dividend paid in relation to the income level (Gustav & Gairatjon, 2012). Plus to use dividend yield, it requires market price of a share in computing dividend yield, which we do not have in our country due to absence of secondary market.

6.3.2 Independent variables

6.3.2.1 Profitability

The decision to pay dividend starts with profit. Therefore, it is logical to consider profitability as a threshold factor, and the level of profitability as one of the most

important factors that may influence firms' dividend decisions. Profitability can be defined as the ability of the firm to create profit (Badu, 2013). The profit size of a firm has been a determinant of dividend policy standing for years. Sheikh Taher (2012) stated that published earnings/profits have long been identified as the primary factor of the firm's capacity to pay dividends. Profit is the single most important factor in a company's financial statement and it has been widely used in previous studies in order to determine the relationship with the company's dividend payout ratio (Gustav & Gairatjon, 2012).

6.3.2.2 Liquidity

Liquidity is usually measured by the firm's cash flow; the cash flow position of a firm is an important determinant of dividend payout. Liquidity is determined based on firm's current asset divided by current liability. According to the agency theory of cash flow, Jensen (1986) argued that firms with high cash flow pay higher dividends in order to diminish the agency conflict between their managers and shareholders. Otherwise, managers may pursue their own personal agenda and maximize their personal wealth instead of maximizing the wealth of its shareholders.

6.3.2.3 Leverage

The term leverage is used to show firms capital structure, mix of debt and equity financing. A firm relies on debt financing in order to minimize agency problem, to tap the tax advantages (interests deduction on income), as a result the use of debt financing can lever-up shareholders' return on equity (Al-Malkawi, 2008). However, leverage entails risk; that is, when a firm acquires debt financing it commits itself to fixed financial charges embodied in interest payments and the principal amount, and failure to meet these obligations may lead the firm into liquidation.

The risk associated with high degrees of financial leverage may therefore result in low dividend payments because firms need to maintain their internal cash flow to pay their obligations rather than distributing the cash to shareholders (Al-Malkawi, 2008), plus an increase in debt in financial industry like bank increases the requirement of reserves by national banks (NBE, 2014).

6.3.2.4 Lagged Dividends

In the real world, it is often believed that companies' pay a steady stream of dividends because investors perceive firms with stable dividends as stronger and more valuable (Maladjian & El Khoury, 2014). Lintner (1956) conducted a study in American firms to test whether current earnings and previous year's dividends have an impact on dividend payout. He found current earning and historical dividends are essential in determining current dividends. Empirical studies have showed a positive relationship between lagged dividends and current dividend payment (Ahmed & Javid, 2008; Yahya & Hadi, 2013; and Maladjian & El Khoury, 2014). Therefore, a positive relationship between lagged dividends and dividend payout is also expected in this study.

6.3.2.5 Growth

Recent experiences have shown that growing firms tend to pay lower dividends. There will be a high demand of capital if a firm is fast growing. The pecking order theo-

ry states that firms should finance new projects first with least information-sensitive sources. Also, firms with high growth opportunities are likely to retain a greater portion of their earnings to finance their expansion projects as against returning these dividends to shareholders (Badu, 2013). Some firms have fewer growth opportunities but tend to pay higher dividends to prevent managers from over-investing the cash available to the firm. In such circumstances, the dividend policy of the firm plays the role of an incentive for the firm to move its resources and hence decrease its agency costs that may arise from the availability of free cash flow funds (Jensen, 1986).

6.3.2.6 Firm Size

Size of a firm has been one of the most commonly used factors in previous studies. Various researchers have argued that the size of the company is one of the factors that has the largest influence on the dividend payout ratio (Holder, Langrehr, & Hexter, 1998).

Information asymmetry between managers and owners/shareholders in large firms are more sensitive than small firms due to lack of close supervision. To control this problem dividend payout is widely used as a motivating factor for managers to show shareholders that their organization is in the right track.

6.3.2.7 Risk

It is argued that business risk is one of the determinants of firm's dividend policy. A firm with stable earnings can predict its future earnings with a greater accuracy. Thus, such a firm can commit to paying larger proportion of its earnings as dividends with less risk of cutting its dividends in the future (Al-Shubiri, 2011). According to the pecking order theory and the trade-off theory, business risk negatively affects the firm's leverage and thus its dividend payout ratio.

Moreover, these theories also argue that firms that are highly risky also experience high cash flow volatility (Al-Malkawi, 2008). As a result firms will be forced to decrease dividend payment.

6. Results and Discussions

The results so far indicated that all CLRM assumptions are not violated, so the ordinary least square regression can be safely applied. However, since this study uses a panel data, there are two types of panel estimator approaches that can be employed for model II, namely: fixed effect model (FEM) and random effect model (REM) (Brooks, 2008). To examine whether individual effects are fixed or random, a Hausman specification test was conducted for model II providing evidence in favor of the fixed effect model (FEM) as presented in Table 4.6, p-value is less than 5%. Therefore, it is rejected that the random effect model is appropriate.

Table 2: Random Effect- Hausman test

	Chi-Sq.	
Test Summary	Statistic	Chi-Sq. d.f. Prob.
Cross-section random	42.434179	0.0000
Source: E-view output		

7.1 Lintner's Dividend Model (Model I)

To replicate Lintner's model in the Ethiopian private banks, the only variables included are profit and lagged dividend paid with dividend payout used as a dependent variable in order to determine whether Ethiopian private banks follow stable dividend payout policy or not using five years data from 2009/10 to 2013/14 for eight sample private banks.

Model I:
$$DVPO_{i,t} = \alpha_i + \beta_1 PRO_{i,t} + \beta_2 LDVP_{i,t}$$

Table 2 below presents the regression results of Lintner's model for the purpose of testing whether Ethiopian private banking sector adhere to stable dividend payout policy. The prediction statement was both profitability and last years' dividend have a significant explanatory power to determine dividend payout. The result shows that the coefficient of lagged dividend paid is positive and statistically significant. This result is similar to the result of numerous studies conducted on emerging markets (Ahmed and Javid, 2009; Kinfe, 2011; and Maladjian & El Khoury, 2014). But profit proxy by earning per share, although it is positive, is statistically insignificant. This finding is consistent with those reported by Aivazian, Booth, & Cleary,(2003); Kinfe, (2011); and Maladjian & El Khoury, (2014)who finds that some emerging capital market firms do not follow a stable dividend payout policy. From this we can conclude that Ethiopian private banks do not follow stable dividend payout policy. The adjusted R² value reveals that the existing model explains 47.8 percent of the dividend payout pattern of Ethiopian private banks. Therefore, hypothesis 8 is rejected, which states that Ethiopian private banks follow stable dividend payout policy.

Table 3: OLS Regression- Lintner's model (Model I)

Dependent Variable- Dividend payout				
Variable	Coeffi- cient	Std. Error	t-Statistic	Prob.
C	43.91962	8.219332	5.343453	0.0000
EPS	0.007725	0.062846	0.122924	0.9028
LDVP	0.538078	0.087743	6.132409	0.0000
R-squared	0.505056		Mean dependent var	92.37105
Adjusted R-squared	0.478302		S.D. dependent var	8.900484
S.E. of regression	6.428699		Akaike info criterion	6.631460
Sum squared resid	1529.142		Schwarz crite- rion	6.758126
Log likeli- hood	-129.6292		Hannan-Quinn criter.	6.677258
F-statistic	18.87797		Durbin-Watson stat	2.366634
Prob(F-statistic)			0.000002	

Source:E-view

7.2 Determinants of Dividend Payout (Model II)

The purpose of Model II is to investigate the determinants of dividend payout in Ethiopian private banks. This is a continuation of Lintner's model by including additional explanatory variables. Five years data were collected from audited financial statements from year 2009/10 to 2013/14 for eight Ethiopian private banks. Dividend payout was used as a dependent variable and seven independent variables: profit, liquidity, leverage, lagged dividend paid, growth, size and risk. A fixed effect model (FEM) panel data regression technique was used to analyze the data based on the Hausman test result.

Table 4 below shows regression results between the dependent variable (dividend payout) and the explanatory variables. The R-square value measures how well the regression model explains the actual variations in the dependent variable (Brooks, 2008). The adjusted R^2 value in table 3 below indicates that 58.73% of the total variability of dividend payout of Ethiopian private banks is captured by the variables in the regression model. Meaning that the seven independent variables; Profit, liquidity, leverage, lagged dividend, growth, size and risk explain 58.73% of the change in dividend payout in Ethiopian private banks for the study period from year 2009/10 to 2013/14.

The regression F-statistic (6.04) and the p-value of zero attached to the test statistic reveal that the null hypothesis that all of the coefficients are jointly zero should be

rejected. Thus, it implies that the independent variables in the model were able to explain variations in the dependent variable.

Table 4: Regression Result- Fixed Effect Model (FEM)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	217.7128	54.21725	4.015564	0.0004
PRO	-0.716192	3.216053	-0.222693	0.8254
LIQ	-0.042386	0.081825	-0.518002	0.6085
LEV	0.612168	0.495490	1.235480	0.2269
LDVP	0.368938	0.101145	3.647629	0.0011
GRO	-0.298105	0.075641	-3.941050	0.0005
SIZ	-14.99256	4.301204	-3.485665	0.0016
RIS	7.878654	2.954011	2.667104	0.0126
R-squared	0.703719			
Adjusted R-squared	0.587323	Durbin-Watson stat	1.272648	
F-statistic	6.045896			
Prob(F-statistic)	0.000057			
Source: E-view output				

The result of the regression analysis showed that profit is not a significant factor that determines dividend payout in Ethiopian private banks. Although this result is against the signaling theory but the insignificant relationship to profit confirms Modigliani and Miller's (1961) assumptions that the value of the firm is independent to the dividend policy and profit does not have an impact on dividend payout. Different researches particularly, studies conducted in developing countries showed insignificant relationship between profit and dividend payout. Liquidity is also found to be insignificant and negative, which is against the theory of agency. Theory of agency states companies that have high free cash flow have high dividend payout ratio to prevent managers from engaging in excessive spending if they have excess free cash flow at their disposal. But contrary to agency theory due to banks their own inefficiency problem they may hold excess liquidity at their disposal which could be used to generate earnings and as a result profit could decrease when liquidity increases. Leverage is also found to have insignificant and positive relationship with dividend payout in Ethiopian private banks. The increase or decrease in leverage has no significant impact on dividend payout in Ethiopian private banks. Banks by their very nature are highly levered firms. They extend loan to borrowers mainly from the deposit they collected from the public. The increase in deposit will lead to the increase in loan granted to borrowers as a result will lead to increase in revenue and profit, and this profit could be distributed to shareholders as a dividend. This case shows that leverage and dividend payout can have a positive relationship. Lagged dividend paid has a significant and positive impact on dividend payout. Banks that pay a high dividend in previous years have a tendency to pay a higher dividend on the coming years holding other things constant, which indicates lagged dividend paid has a positive impact on current year's dividend payout.

The variable growth has shown a significant and negative relationship with dividend payout. This finding supports the pecking order theory which says that the companies should use first internal sources to fund different projects and to keep the company growth. Therefore, firms with high growth or investment opportunities tend to retain their income to finance their investments, thus paying less or no dividends. Ethiopian banking industry is in growth stage and these private banks require further investments to fund the growth and the best alternative for financing this with low cost of capital is to use the profit the banks are generating than distributing it as a dividend. This implies that growth and dividend payout has an inverse relationship. Size is found to have a significant but a negative impact on dividend payout against the theory of agency, which describes large firms face high agency costs as a result of ownership dispersion, increased complexity, and the inability of shareholders to monitor the firm activity closely. Hence, such firms pay a larger dividend to reduce agency costs. Risk is also found to have a significant and positive relationship with dividend payout. The finding showed that the increase in risk will lead to the increase in profit; this finding is against the finding of many researches and could be attached to industry or country factors.

8. Conclusion

Studying the factors that determines dividend payout has a significant importance in the business world where there are a lot of public companies that acquire capital from the public and distribute dividends from the profit they make. The main purpose of the study was to examine the determinants of dividend payout in Ethiopian private banks and testing Lintner's model in Ethiopian context to check whether Ethiopian private banks follow stable dividend payout policy or not. In order to meet the purpose a five years financial statement data were used from audited financial statements of the banks and National bank of Ethiopia reports from year 2009/10 to 2013/14 for eight selected private banks. The collected data was analyzed using pooled Panel regression method for model I and fixed effect panel regression method for model II.

Pooled panel regression method is used for model I to test whether Ethiopian private banks follow stable dividend payout policy or not. The result showed that Ethiopian private banks did not follow stable dividend payout policy. Rather they change their policy from time to time based on existed condition and this situation may affect shareholders who prefer stable dividend payout policy to divert their investment to other companies who have stable dividend payout policy.

Fixed effect panel regression method was used for model II in order to examine the relationship between the seven company specific factors, which are (profit, liquidity, leverage, growth, size and risk) and dividend payout. The result of the regression analysis showed that profit, liquidity, and leverage are not a significant factor that determines dividend payout in Ethiopian private banks. But lagged dividend, growth, size and risk have a significant impact on dividend payout in Ethiopian private banks.

9. Recommendation

The below recommendations are forwarded based on the finding of the research:

Investors who want to invest on Ethiopian private banks and prefer stable dividend

payout need to consider that Ethiopian private banks do not necessarily follow stable dividend payout policy rather they change their policy from time to time based on different factors.

To make an informed decision on investment options, investors need to look at how was the banks performance in the following factors; lagged dividend paid, growth of the bank, size and risk factors before making an investment decisions. Because these factors have a significant impact on dividend payout in Ethiopian private banks.

Board of directors of banks need to consider lagged dividend paid to set future dividend payout because shareholders expect banks that have a track record of paying high dividend is expected to pay higher dividend in the coming year. They also need to consider the growth of their banks which affects the fund available to distribute to shareholders due to growing banks consume larger portion of their profit to finance the growth. Size and risk variables have also significant effect on dividend payout. So, board of directors also needs to consider these variables while deciding their dividend payout policies.

The current relative conducive environment for investment as a result of the establishment of many share companies is an option for investors in addition to the financial sector. Absence of stock market (Secondary market) where investors can easily sell or buy shares of companies and related high costs to investors to sell shares to generate money may require high dividend by investors since it is the only option to be benefited from their investment in short period of time. Therefore, Private Banks should work to retain and attract investors by paying high dividend than other industries. Otherwise, there could be a possibility for shift of capital to these new corporations that pays high dividend.

A research conducted on this subject is very few in Ethiopian banking industry to test empirically the determinants of dividend payout. Therefore, it may help future studies in the subject as a reference.

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