

**EFFECT OF DIVIDEND POLICY DECISION ON FINANCIAL PERFORMANCE
OF PRIVATE MANUFACTURING FIRMS IN NAIROBI CITY COUNTY**

^{1*}Edwin Krop Komolng'ole & ²Dr. Nathan Mwenda

^{1*}Scholar, Kenyatta University

²Lecturer, Department of Accounting and Finance, Kenyatta University

Accepted September, 15th, 2023

ABSTRACT

The study sought to establish the effect of dividend policy decisions on financial performance of private manufacturing firms in Nairobi City County. The study was guided by the Dividend Irrelevance Theory. The study employed a descriptive research design. The population for this study consisted of 455 enrolled private assembly enterprises. The five-year period under consideration was from 2016 to 2021. Using Krejcie and Morgan (1970) formula sample size of 208 was determined. The data was sourced from two primary sources - the finance department of the institutions and the Kenya Association of Manufacturers website. The data was coded, transformed for analysis through the use of STATA software for statistical analysis. The study found that dividend policy has a positive and significant effect on financial performance of private manufacturing firms in Nairobi City County. Higher levels of dividend policy were found to lead to an increase in financial performance. The study recommends for firms to have a healthy level of retained earnings to support their future growth and investment initiatives. Firms should also consider their financial position and other factors when making dividend decisions to ensure they are sustainable.

Keywords; *Dividend Policy Decision, Financial Performance Private Manufacturing Firms*

INTRODUCTION

Financial management is an indispensable part of dealing with the tasks of any firm. It plays a critical role in the management of an organization's resources. The kind of assets a company owns determines how that company will develop throughout the course of those assets' long lives. If a company cannot responsibly plan and establish a strategy to efficiently manage its finances, it may not be able to view the long term. As a result, the fundamental issues that major corporations have are primarily caused by inefficient financial management overall (Jindrichovska, 2003).

Financial management is the planning, directing, organizing, and control of all financial activity inside a company. These actions could entail the acquisition and application of enterprise resources. "Financial management" is the process of applying general management ideas to an organization's financial resources (Weston and Brigham, 1996). Financing, asset management, and investment decisions make up the three main components of the decision function in financial management, which is the embodiment of these disciplines. Because financial action must be evaluated in the context of some standard in order to be effective, financial management necessitates the existence of an existing target or goal.

Authors and experts have pushed toward specific areas of monetary administration in various ways, giving their area of focus full attention. For example, a survey finished in Malaysia by Mohd et al. (2010) showed that the pieces of monetary administration contained monetary bookkeeping, monetary preparation and control, monetary examination, management bookkeeping, capital planning, and working capital administration.

Chung and Chuang (2010) focused on five specific areas of monetary administration practices: monetary reporting, capital design management, working capital administration, and analysis, capital planning, and bookkeeping data framework. From the survey factors, Funding, Financial planning, and resource board choices work out. Deresse and Prabhakarai (2012) utilized free factors like revealing, bookkeeping, and examination, working capital administration, fixed resource management, and financial wanting to address financial management practices in the focus on the impact of financial management practices and qualities on benefit in Ethiopia. Different factors that they considered were Liquidity, Influence, and resource turnover.

Kieu (2006) utilized financial management rehearses factors like bookkeeping data framework, working capital administration, fixed resource management, monetary preparation, monetary revealing and examination, and great execution in monetary qualities like liquidity and business movement. Hence, the survey emphasized four vital factors to address financial management rehearses that have been liquidity choice that actions the degree of which an association has adequate money to meet its quick and transient monetary commitments also satisfied by Bhunia (2015). It can also be defined as the ability of an indebted person to take care of their obligations as and when they fall due.

The use of borrowed money and debt financing in an effort to improve a business's operations and profitability is known as financial leverage (Pandya, 2019). Investment approach decision: this entails deciding how much money to commit to long-term assets that will produce advantages in the future (Effiong, 2013) is the most recent example. The firm's dividend policy determines whether earnings should be distributed as dividends or reinvested back into the business (Mitton, 2004).

The term 'Performance' is derived from the word 'parfourmen,' and that means 'to do,' 'to complete,' or 'to deliver.' Performance alludes to the act of performing performance, satisfaction, and achievement. In a broader sense, performance alludes to the accomplishment of a given errand measured against preset principles of fulfillment, cost exactness, and speed. As such, it alludes to how much an achievement is being achieved.

Financial performance can be particular as a close-to-home extent of how well a firm can use assets from its fundamental strategy for business and produce compensations (Plants, 2008). This term is in like manner used as a general extent of a business' overall money related prosperity throughout a given time period and can be used to associate near firms across a comparative industry or to check out associations or regions in a gathering. The display perspective thought demonstrates the way that laborers can grow the value of the firm by; extending the size of an organization's future earnings, by restoring the receipt of those salaries, or by making them more convinced or more secure (Cadbury, 1992).

There are various ways of estimating financial, yet all methodology ought to be taken in collection. A portion of the pointers of financial performance are return on value, liquidity proportions, resource the board proportions, benefit proportions, influence proportions, and market esteem proportions.

Carretai and Farinai (2010) guarantee that utilization of financial performance may as yet be legitimate in light of the fact that it reflects what supervisors really reflect to be monetary performance and, regardless of whether this is a combination of different pointers like bookkeeping benefits, efficiency, and income. Financial performance is determined by the resulting pointers: benefit or worth added, deals, charges, spending plan expenses or consumption and securities exchange markers (for example, Share cost) and independence. Intermediaries for the monetary exhibition likewise incorporate the bookkeeping proportion of execution; return on value (ROE) and return on resource (ROA).

Businesses in the manufacturing industry are those that manufacture and process goods to create new products or enhance existing products (Lawrence & Chad, 2012).

In Kenya, private manufacturing organizations have turned into a crucial support of the economy. The manufacturing area adds to the public target of creating work open doors and generating pay for the economy (Njoroge, 2014). The manufacturing area leads in unfamiliar trade acquiring for the nation representing 34% of the complete profit (Kenya Association Makers (KAM, 2014). The KAM is an enrollment bunch whose job is to offer initiative and administrations pointed toward upgrading the development of a serious manufacturing area in Kenya.

In Kenya, the manufacturing unit is supposed to keep being a lively and solid support of the supported recuperation and development of the Kenyan economy (Kungu, 2015). A larger part of manufacturing organizations in Kenya utilizes up to 100 specialists (GOK, 2015). The manufacturing section stays the significant wellspring of work open doors, representing around 20% of the absolute business or 2,105,000 people in 2013 (GOK, 2014).

As a huge area in the general financial development, manufacturing area needs a top-to-bottom examination at industry as well as firm level. The manufacturing business in Kenya is overwhelmed by auxiliaries organizations of multinationals. The players fall into the accompanying classifications as addressed in the Kenya relationship of production's postings: food and drinks handling, Wood items Drug and clinical hardware, Endlessly paperboard, Cowhide items, Compound and united, Materials, Tobacco, Plastics, and elastomers (Relationship of Makers, 2013). Producing is a significant support of the economy as it contributes 10% of Gross domestic product, 12.5% of Commodities, and 13% of formal business (CBK, 2013).

Kenya is a vital objective for financial backers who are quick to place their cash in manufacturing. While the nation isn't supplied with the mineral abundance that most of its neighbors display, it more than compensates for it, because of the accompanying: perhaps the best representative in Africa, a productive horticultural area, and consequently a reliable wellspring of crude components for agro-based manufacturing, a genuinely versatile monetary administrations area, bankable broadcast communications, and vicinity to port offices. An extraordinary many open doors for immediate and joint endeavor ventures exist in the manufacturing area including handling, production of pieces of clothing, plastics,

synthetic substances, drugs, metal designing items for neighborhood, gathering of car parts, hardware, and commodity markets (Republic of Kenya, 2018).

Kenya's manufacturing industry, which accounts for 10% of the GDP and hence has the largest impact on the nation's economic growth, is a crucial sector for the nation. There are over 2600 manufacturing businesses nationwide (KAM, 2018). Kenya is ranked top among the EAC member countries for having the most advanced manufacturing sector, according to KAM (2018). Because of its colossal potential to produce pay, make occupations, create unfamiliar trade, draw in unfamiliar speculation, and ease destitution in the general public, Kenya's manufacturing area fills in as the foundation of the country's financial turn of events and development (Vocalist, 2017).

1.2 Statement of the Problem

The manufacturing sector in Kenya is enormous and contributes significantly to economic growth, progression, and productivity. However, many manufacturing organizations have moved or restructured their operations, choosing to serve the local market through importing from low-cost producing regions like Egypt, South Africa, India, and even China, thereby resulting in job losses (Kariithi and Kihara, 2016), consequently denying the country 100 billion annually. This is an indication that many manufacturing firms in Kenya are experiencing performance challenges, with many issuing profit warnings due to difficulties in the operating environment (GoK, 2017). Data from the World Bank shows that manufacturers operating in Kenya registered stagnation and declining profits throughout the past five years due to a challenging operating environment (World Bank, 2017). The manufacturing sector in Kenya contributed only 13.6% to the GDP in the year 2016, indicating a decline from the previous year 2015, where it had recorded a 5.6% growth (KNBS, 2017).

In Kenya, most private manufacturing firms are struggling to operate, while others have been forced to shut down, and others are operating at the break-even point. If this trend continues, the aspiration of rising to a middle-level economy is thwarted. The manufacturing sector employs around 20% of the total workforce of approximately 12 million workers (Kenyan Workers Assessment, COTU, 2018) in the economy (Kung'u, 2015). Improvement of the organization's worth is certainly not a straightforward commitment since it includes the decision of commitment and worth participants in a fair rate, considering different costs and

related benefits. It is noteworthy that wrong financial management practices decisions could cause an organization's financial distress that may eventually lead to Chapter 11 (Owolabi, Inyang, and Uduakobong, 2017).

There is a need to understand the effect of financial performance on private manufacturing firms. Predominant performance reflects the leaders' capability and efficiency in using the company's profits, and this, in turn, adds to the country's economy at large (Kung'u, 2015). Kiarithai (2016) organized a positive association between financial performance and access to funds. Bunyasi, Namusonge, and Bwisai (2014) argued that access to pioneering cash strongly influences the performance of SMEs. Kinyanjui (2015) found a positive association between access to financial capital and firm performance. Similarly, Nanagaki and Namusonge (2014) argue that there is a positive association between access to finance and the performance of ventures associations.

Moreover, Gupta, Srivastai, and Sharma (2015) suggest that organizations that have high profits and good performance have less commitment. Ummar, Tanveer, and Aslam (2014) in their study on the effect of capital structure on financial performance in Pakistani concluded that capital structure decision is a significant element of financial performance of firms. Javed and Akhtai (2016) organized a positive relationship among impact, financial performance, and growth. Okelo (2016) claims that capital structure influences the financial performance of organizations. Past work on performance in Kenya just revolved around business performance of small and medium enterprises (Namusonge, 2017). Otieno (2017) suggests that expansion strategies affect the performance of Kenya's manufacturing associations. Wawire (2015) suggests that tax collection was negatively associated with financial performance as it increases the cost of running business. Mwangi (2016) claims that venture financing was positively connected with financial performance. The lack of assessments focusing on financial performance in the private manufacturing sector prompted me to conduct this review. This study aimed at laying out the financial performance and financial management practices of private manufacturing firms in Nairobi City District. The extent of organization performance would be a mixture of both financial and non-financial measures. Financial measures can be represented by profit, returns from investment (return on investment), returns on value (ROE) income, and profit per share (EPS) (Omar, 2017).

They participate in the advantage of being objective, clear, and straightforward. Nevertheless, they have the disadvantage of being not very accessible and being obvious, thus providing only loose information. They can also be reliant upon manipulations and inefficiency (Ng'ang'a, 2017). Non-financial measures include the number of employees, customer satisfaction, employee satisfaction, income growth, income per employee, and market share. Non-financial measures have the weakness of being subjective (Njeru, 2015). Because of the limitations of the non-financial measures and financial, the review will utilize a mixture approach combining both financial and non-financial performance measures. It is therefore that this study was aimed at laying out the financial performance and financial management practices of private manufacturing firms in Nairobi City Province.

Objective of the Study

The overall objective of the research was to establish the effect of dividend policy decision on financial performance of private manufacturing firms in Nairobi City County.

LITERATURE REVIEW

Ever since business organizations first started to exist, profit strategy has been a topic of interest in financial literature. The phrase "profit strategy" refers to a method for determining how much of a firm's earnings is distributed to its investors. According to Namachanjai (2016), profit strategy refers to a long-term financial plan on how to increase the income generated by the firm's operations while making decisions on the rate allocated to investors as profits (Ndirangu, 2014). Profit strategy is described as the rules and principles that an organization uses to decide to allocate profit portions to financial backers. The benefit strategy selections of associations are a fundamental part of corporate game plan.

Benefit strategy is ordered into four basic sorts. The first kind of benefit strategy is known as a standard benefit strategy where financial backers are conveyed benefits on average ranges. This arrangement applies to firms that have normal and stable income. The second benefit strategy is Consistent benefit strategy where financial backers get benefits in an anticipated way from one period then onto the next. This methodology is partitioned into three designs: consistent remuneration out extent, consistent benefit per share, and low standard notwithstanding extra benefit. For firms with predictable compensation, they lean toward a stable benefit strategy known as consistent benefit per share where consistent benefit per share is paid regardless of fluctuations in the firm's net profit. On the other hand, firms with

unstable compensation lean toward stable benefit technique known as low standard notwithstanding extra benefit (Shisia, 2014).

The third sort of benefit strategy is inconsistent benefit technique; here, financial backers don't get ordinary benefits from the associations, and the strategy is applied when pay is uncertain, futile undertaking, lacking liquid resources, and inconvenience of adverse effects of consistent benefit on the money related execution of the affiliation. The fourth benefit strategy is no benefit technique; a couple of associations take on a game plan of not conveying benefits considering its inconvenient money related position or when capital is required for speculation purposes like expansion and improvement. While going with the decision of how much compensation to disperse as benefits, finance managers need to review that enhancing financial backers' regard is the organization's key objective (Khorsandi, 2013). Benefit strategy was apportioned using benefit pay extent in the audit.

The benefit strategy embraced by a firm and its effect on their performance remain an enigmatic and examined issue groundbreaking. The Plant administrator and Modigliani express that benefit procedures don't influence the valuation of a firm, particularly in an optimal market. However, prevailing investment battles that financial backers can use benefit pay-out to anticipate the organization's future financial performance considering the signs that come from the statements of benefits. The bird nearby speculation confirms that the relationship associating firm valuation is still up in the air by a solitary monetary sponsor's tendency of benefits rather than capital augmentations. While the workplace speculation battles that high benefit payout prompted a decrease in association costs, further developing association productivity. Financial execution of most firms deals with subsequent to conveying benefits; thus, there is a connection between the financial performance of a firm and benefits paid (Barnor, 2014).

Theoretical Framework

The study was guided by the Dividend Irrelevance Theory. The Dividend Irrelevance Theory is a concept in finance and investment theory that was developed by Franco Modigliani and Merton Miller in the 1960s. This theory suggests that, under certain assumptions, the dividend policy of a company should not affect its stock price or its overall value. In other words, investors should be indifferent to whether a company pays dividends or retains its earnings to reinvest in the business (Miller, 1988). The theory assumes that capital markets

are perfect, which means that investors have access to all relevant information, transaction costs are minimal, and there are no taxes or other frictions that would affect investment decisions. It assumes that investors have no preferences between receiving dividends and capital gains (the increase in stock price). In other words, investors are only concerned with the total return on their investments. The availability of profitable investment opportunities is a critical factor. If a company can reinvest its earnings at a rate of return that exceeds the required rate of return demanded by investors, then retaining earnings and not paying dividends is considered optimal. The theory ignores the impact of taxes on dividends and capital gains. In reality, taxes can affect investor preferences and the overall value of a company. The theory assumes that companies can always raise external funds (debt or equity) at the same cost as their internal funds. In reality, external financing may come with higher costs and restrictions (Bhattacharyya, 2007).

METHODOLOGY

The study employed a descriptive research design. The population for this study consisted of 455 enrolled private assembly enterprises. The five-year period under consideration was from 2016 to 2021. Using Krejcie and Morgan (1970) formula sample size of 208 was determined. The data was sourced from two primary sources - the finance department of the institutions and the Kenya Association of Manufacturers website. The data was coded, transformed for analysis through the use of STATA software for statistical analysis.

FINDINGS AND DISCUSSION

Descriptive Statistics

In this study, descriptive statistics entailed calculation of standard deviation, mean, maximum and minimum of dependent variable and the independent variables. The data was collected from 208 privately owned manufacturing firms in Nairobi county. The study collected data from year 2016 to year 2021.

Table 1: Descriptive Statistics

Variable/Ratio	Obs.	Mean	Std. Deviation	Min.	Max.
Profitability (ROA)	1040	0.147	0.163	-3.135	2.484
Dividend Policy (Dividend payout ratio)	1040	0.488	1.696	0.112	0.846

On profitability which was measured in terms of ROA, the findings in Table 4.1 show that the mean return on Asset (ROA) is 0.147, with a standard deviation of 0.163. The minimum

ROA is -3.135 and the maximum is 2.484. An indication that some of the privately owned manufacturing firms in Nairobi county were profitable while others incurred losses. On average, it indicates that the privately owned manufacturing firms in the sample have modest profitability, with the average firm having an ROA of 0.147. The importance of ROA in measuring a firm's profitability cannot be overstated. Research has shown that higher levels of ROA are associated with higher market valuations and lower levels of financial distress (Susanti, Latifa & Sunarsi, 2020). The dividend payout ratio is a significant measure of a firm's financial performance as it represents the portion of earnings paid out as dividends to shareholders. In this study, the dividend policy variable was measured using the dividend payout ratio for privately owned manufacturing firms in Nairobi County between 2016 and 2021. The average dividend payout ratio for the sampled firms was 0.488. This implies that, on average, the firms paid out almost half of their earnings as dividends to shareholders. However, the findings also indicated a large standard deviation of 1.696 in the dividend payout ratio, suggesting significant variations in dividend policies across the sampled firms. This finding is consistent with previous studies that reported significant variations in dividend payout ratios across firms and over time (Baker & Powell, 2009; Eriotis et al., 2011).

Trend Analysis

Profitability

The Return on Asset (ROA) is a financial metric that measures a company's ability to generate profit relative to its total assets. A high ROA indicates that a company is using its assets efficiently to generate profit, while a low ROA indicates that a company is not generating sufficient profit with its assets. Trend analysis for profitability (ROA) can be used to examine a company's ability to generate profits relative to the amount of total assets invested in the business over time. The ROA is calculated by dividing net income by total assets.

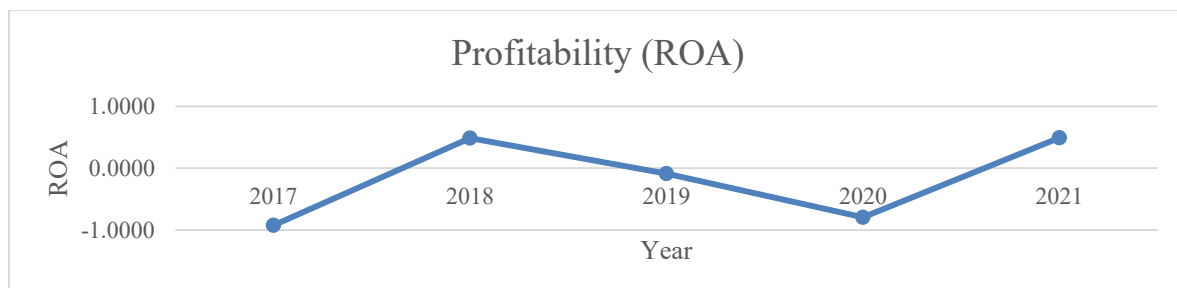


Figure 1: Trend Analysis for Profitability

The Return on Asset (ROA) is an important financial metric that measures a company's ability to generate profits from the assets invested. The fluctuation of ROA over time is crucial to understanding a company's financial performance. The data shown in Figure 4.1 reveals that the company's ROA has varied significantly over the years. According to the data, the company started operating at a loss in 2017 with an ROA of -0.9232. However, the ROA improved in 2018 to 0.4859, indicating that the company started generating profits. But the ROA dropped to -0.0884 in 2019, indicating that the company was unable to generate sufficient profits to cover the assets invested. This trend continued in 2020, with the ROA dropping to -0.7938, indicating a loss for the company. However, there was a significant improvement in 2021, with the ROA increasing to 0.4907, indicating that the company was generating more profits relative to the assets invested. The study by Alarussiiand Alhaderi (2018) supports the importance of profitability in determining a company's market valuation and financial distress levels. They found that companies with higher profitability tend to have higher market valuations and lower levels of financial distress. Therefore, it is crucial for companies to maintain a healthy level of profitability, which can be measured through metrics such as ROA, to ensure long-term financial stability and success.

Dividend Policy

The dividend payout ratio represents the portion of earnings paid out as dividends to shareholders. Figure 2 presents trend analysis for dividend payout ratio for privately owned manufacturing firms in Nairobi County between 2016 and 2021.

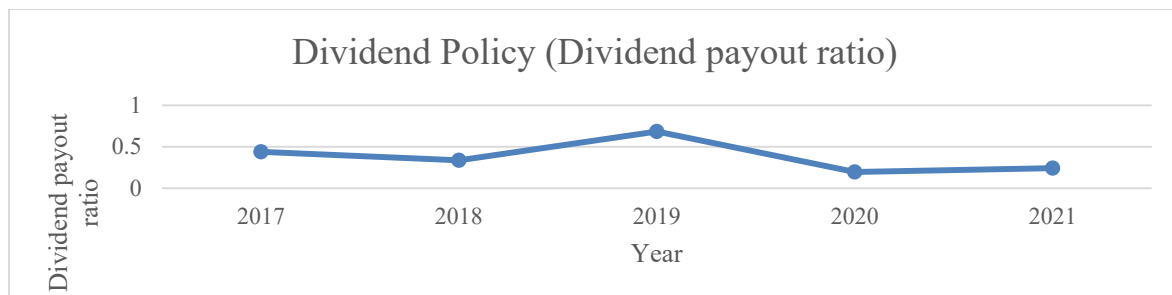


Figure 2: Trend Analysis for Dividend Policy

The trend analysis of Dividend Policy (Dividend payout ratio) for the selected privately owned manufacturing firms in Nairobi County between 2016 and 2021 shows a fluctuating pattern. In 2017, the dividend payout ratio was 0.439, indicating that the firms distributed

43.9% of their earnings as dividends to shareholders. However, in 2018, there was a decrease in the dividend payout ratio to 0.336, which suggests that firms reduced the proportion of earnings distributed as dividends to shareholders. The dividend payout ratio increased in 2019 to 0.683, showing that firms distributed a higher percentage of earnings as dividends. However, in 2020, there was a significant drop in the dividend payout ratio to 0.196, indicating that firms reduced the percentage of earnings distributed as dividends. In 2021, the dividend payout ratio slightly increased to 0.242.

The fluctuating pattern of the dividend payout ratio may be due to various factors, such as the firm's financial performance, investment opportunities, and liquidity needs (Allen & Michaely, 2003). Additionally, changes in tax policies and regulations can also influence the dividend payout decision of firms (Dhaliwal, Erickson, & Frank, 2019). The literature suggests that dividend payout ratios can impact a firm's cost of capital and valuation (Jain & Kini, 2015), and firms with high dividend payout ratios may experience lower earnings growth (Baker, Farrelly, & Edelman, 2018). Therefore, it is important for firms to strike a balance between dividend payouts and retaining earnings for reinvestment to maintain long-term growth and profitability.

Correlation Analysis

The correlation coefficient is a widely used tool in statistical analysis to quantify the strength and direction of the relationship between two variables.

Table 2: Correlations Coefficient

		Profitability
Profitability (ROA)	Pearson Correlation	1
	Sig. (2-tailed)	
	N	1040
Dividend Policy	Pearson Correlation	.737**
	Sig. (2-tailed)	.009
	N	1040

** . Correlation is significant at the 0.01 level (2-tailed).

The correlation coefficient between profitability and dividend policy is 0.737 ($p < 0.01$), indicating a strong positive relationship between the two variables. This suggests that firms that pay higher dividends tend to have higher profitability. However, this finding is not

supported by all studies, as some studies suggest that retaining earnings and reinvesting them in the firm can lead to higher profitability in the long run (Kumar and Singh, 2018).

Conclusions

The study concludes that dividend policy has a positive and significant effect on financial performance of private manufacturing firms in Nairobi City County. Higher levels of dividend policy were found to lead to an increase in financial performance. This finding was consistent with previous studies that suggest that dividends can be a signal of firm profitability and stability.

Recommendations

The study found a positive relationship between dividend policy and financial performance. Therefore, firms should consider adopting a dividend policy that rewards their shareholders while maintaining a healthy level of retained earnings to support their future growth and investment initiatives. However, firms should also consider their financial position and other factors when making dividend decisions to ensure they are sustainable and do not negatively impact their financial performance.

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