SMC UNIVERSITY
Swiss Management Center – Transknowlogy Campus

Kesete Abraha Hadgu

# Primary reasons for dividend reduction/omission and the relationship between dividends and earnings, share prices, assets and liabilities among Kenyan companies quoted on the Nairobi Stock Exchange

## Abstract

Over the past half a century, no consensus has been reached on the dividend behavior despite numerous studies having been carried out by various researchers. Even in the advent of the 21st century, the issue of dividend behavior has been receiving growing interest among both academic and industry researchers. In the Kenyan context, few studies have been conducted on dividend behavior and most of the studies were limited in scope, hence the need for this study. The study focused on two objectives. The first objective was to investigate the relationship between dividends and earnings, share prices, assets (current & non-current) and liabilities (current & non-current) in the short and long terms. The second objective was to examine the joint influence of earnings, assets & liabilities on dividends in the short and long terms. To achieve the above objectives five research questions and five hypotheses were formulated. The study adopted quantitative research method and purposive sampling strategy. The primary data was collected using questionnaire while the secondary data was collected from published financial statements from 34 and 35 respectively from a population of 57 listed companies on the NSE. The data was analyzed using SPSS and Excel spreadsheets with the main analysis tools being descriptive statistics, correlation and regression analysis. The findings were presented using tables and charts. The study investigated the relationship between dividends (at time t-1 and t) and earnings (at time t-1 and t) and the correlation was weak in both the short (-2 to +2) and long (1993 to 2010) terms except at the dividend reduction/omission period (t=0) and in the 2 years after the dividend reduction/omission period (+1 to +2). Dividends (at time t-1 and t) and share prices (at time t) were positively and strongly correlated both in the short and long terms and particularly it was the highest in the 2 years before the dividend reduction period. The relationships between dividends and assets & liabilities were examined and no correlation was established. In addition the joint influence of earnings, assets & liabilities on dividends was investigated and it was found that only earnings, non-current assets and non-current liabilities were jointly correlated with dividends, albeit the influence of the assets and liabilities were very limited. The general conclusion drawn from the study was that managers consider numerous factors including earnings to determine dividend payout levels. However, despite the fact that dividends were weakly correlation with earnings except at the dividend reduction/omission period and in the 2 years after the reduction periods where the correlation was moderately strong, investors showed sensitive reaction to dividend changes. This was manifested by the strong correlation between dividends and share prices and this was consistent with the findings conducted in and outside Kenya. However, the dividend signaling theory had found limited support in the Kenyan context and it is recommended that investors should exercise great caution in using dividends and share prices to gauge financial performances and should seek for more information before they make investment decisions.