

**EFFECT OF DIVIDENDS POLICY ON FINANCIAL PERFORMANCE OF FIRMS  
LISTED ON THE RWANDA STOCK EXCHANGE**

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**ABSTRACT**

This study sought to appraise the effect of dividend policy on financial performance of firms listed on RSE. Both primary and secondary data were used by the study. The study adopted descriptive research design and the population was all the six companies listed in the Rwanda Stock Exchange (RSE). A census survey was conducted on all the six listed firms and purposive sampling technique was used to sample the respondents to participate in the study. Data was analyzed using descriptive statistics, correlation analysis and regression analysis using SPSS version 20. The study findings indicated that dividend policy is positively associated with ROA. Furthermore, dividend policy is positively associated with ROE. The regression results indicated that the relationship between dividend policy and both ROA and ROE is positive and significant. Based on the study findings, the study concluded that dividend policy is positively and significantly associated with both ROA and ROE and that dividend policy explains a larger change in ROE than in ROA. Furthermore, the study also concluded that dividend policy is positively and significantly related to both ROA and ROE. In general, dividend policy is positively and significantly related to financial performance

of firms listed at the RSE. The study recommends that firms listed at the RSE should improve their dividend policy as it leads to improved financial performance. The firms should operate under established and regularly observed dividend policy and also pay dividends in correlation with its value.

**Key words:** *Dividends policy, financial performance, Rwanda stock exchange, ROA, ROE*

## **INTRODUCTION**

### **Background and Research Gap**

Financial aspect is a concern over the world. Panu, Andrew & Erik (2006) and Goergen (1999) argue that there is a relationship between corporate governance, ownership and financial performance. Furthermore, Sandra & Samuel (1999) indicated that there is a positive association between financial performance and Corporate Social Performance supporting the theory that slack resource availability and Corporate Social Performance are positively related. According to the scholars, corporate social performance is also positively associated with future financial performance, supporting the theory that good management and Corporate Social Performance are positively related.

The Corporate sector growth is essential to economic development. And the corporate finance pattern of the company is vital importance for the financial wellbeing of companies in any sector. Corporate finance decisions affect the various areas of the corporate management, which determine the wealth of investors. Public sector of Sri Lankan corporate finance decisions accomplishments affects not only the financial soundness of the concerned Private Equity but also the financial health of the nation as a whole, while these are essentially public investment decisions of the government and a number of Sri Lankan Government agencies are involved in this process ( Sritharan, 2014).

In Ghana, studies have been done on how dividend policy affects financial performance of the firm on Ghana Stock Exchange. Samuel & Edward (2010) examined the relationship between dividend policy and financial performance of banks in Ghana. The study used panel data constructed from

the financial statements of 16 commercial banks in Ghana for a period of 5 years, from 1999-2003. The result was in tandem with earlier studies that dividend policy had an effect on firm value.

Rwanda is member of East African Community and has trade relationship with free commerce, property and personnel movement with the members. Whatever happens to one as far as development is concerned usually affect the other. They are more or less partners and progress rather than competitors in business.

Development programs in the communities' countries often follow the same pattern eg. 2020 development in Rwanda and 2030 program in Kenya. Even the program initiative and content are similar. Like many of their policies, constitution and institution including financial system.

A Financial market is where securities are bought and sold at prices governed by the forces of demand and supply. Stock exchanges impose stringent rules, listing requirements, and statutory requirements that are binding on all listed and trading parties

In Kenya, There are more than 50 businesses and companies listed in the Nairobi Stock Exchange, including Sasini Tea and Coffee Ltd., Kenya Airways, Jubilee Insurance, Kenya Commercial Bank Ltd., and Ken Gen Ltd. Most of the businesses in the exchange are in the financial or industrial sectors, though agriculture and other commercial services are also represented. Also listed are treasury bonds issued by the Government of Kenya. Occasionally, there are also privately issued corporate bonds as well. Trading takes place 5 days a week (Monday to Friday) but only between the hours of 10am and 12 noon. (Wikipedia 11/11/2014)

### **Problem Statement**

Capital market consists of market for medium and long term funds. This is typicalized by stock exchange like Rwanda stock Exchange. This is the trading floor for company securities and it is divided into two. Market for initial securities called primary market and market for traded securities called secondary market. In essence the market is where shares are issued and traded among investors. The government of Rwanda has a goal to develop the economy by 2020 therefore it has to encourage participation and growth of the stock market, thereby facilitating the growth, flow, and regulation of the stock market. The government ensures that investors are protected, it also advises and guides companies seeking capital and provide an important infrastructure and conducive environment for business development.

Despite the government efforts, the capital market is not growing at the pace expected. Should the slow development of the stock market persist then the growth and development target for the year 2020 may be difficult to achieve. Need therefore arose to identify, appreciate and work assiduously on the factors that determine financial performance of firms listed on the Rwanda Stock exchange.

Studies conducted to examine the factors affecting financial performance of listed firms have mostly looked at the variables used in the current study in isolation of each other thus creating a conceptual research gap. No study has combined capital structure, dividend policy, corporate governance and timely rendition of information to investigate financial performance of listed firms. For example, a study was conducted by Nikolaus (2015) to examine the determinants of firm performance of Indonesian and Dutch firms over the period of 2009-2013. The study however focused in Netherlands. Kungu, Ayako and Githui (2015) conducted a study to analyze the factors affecting the performance of 41 non-financial companies listed on the Nairobi Securities Exchange (NSE) using panel data over the period 2003 to 2013. The study however used panel data and looked at Nairobi securities exchange. A study was conducted by Vintila and Nenu (2015) to analyse the determinants of corporate financial performance of Bucharest Stock Exchange Listed Companies and it presented a contextual research gap because it was conducted in Bucharest. Furthermore, Mwangi and Murigu (2015) conducted a study to establish the factors that affect the profitability of general insurers in Kenya and the study presented a contextual research gap since it focused on insurance. Mwangi, Muathe and Koimbei (2014) also investigated the relationship between capital structure and financial performance of non-financial companies listed in the Nairobi Securities Exchange (NSE). The study however used only one variable which is Capital structure. Another study was conducted by Vincent (2011) to investigate the effects of ownership structure on performance of listed companies in Kenya but it only focused on corporate governance. A study by Uwalomwa, Jimoh and Anijesushola (2012) investigated the relationship between the financial performance and dividend payout among listed firms' in Nigeria while focusing on dividend policy only. Velnampy and Vickneswaran (2014) on the other hand examined the significant impact of capital structure (CS) and liquidity position (LP) on profitability of listed telecommunication firms in Colombo Stock Exchange (CSE). The study also focused on capital structure and liquidity position only. It is due to these conceptual research gaps that the current study combined the variables and also adds another variable which is timely rendition of information beyond statutory time so as to obtain a more comprehensive analysis of determinants

of financial performance of listed firms. The study also aimed to fill the contextual gaps arising as a result of different scopes under which the reviewed studies were conducted since they were not conducted in Rwanda nor focused on the firms listed on the Rwanda stock exchange. The current study hence sought to assess determinants of financial performance of firms listed on the Rwanda Stock Exchange.

Many determinants influence the financial performance of firms listed on Rwanda Stock Exchange. These include: dividend policy, capital structure, corporate governance, timely rendition of information others are: function leverage, hedging, financial risk, risk tolerance, risk evasion, financial literacy, liquidity, ability to invest, etc. However for the purpose of this study, the study focused on the first determinant because it is assumed that in Rwanda they seem to play high role in financial performance. The study hence established the effect of dividends policy on financial performance of firms listed on the Rwanda Stock Exchange.

### **Study Objectives**

The general objective of this study was to assess the effect of dividend policy on financial performance of firms listed on the Rwanda Stock Exchange

### **RESEARCH METHODOLOGY**

The research design adopted for the study was descriptive survey design. The target population for this study was the firms listed at Rwanda Stock Exchange (RSE) as at the year 2014. By the end of the year 2014, there were 6 firms listed at the Rwanda stock exchange. A multi stage sampling approach was used where sampling was done at the unit of analysis level and at the respondent's level. The unit of analysis was the firms listed at the Rwanda stock Exchange. At this level, all the 6 firms were used in the study. This is a census approach. Sampling was also done at the respondent's level. The respondents were management staff from the Operations, Finance and Accounts departments. The study purposively sampled 4 staff members from each department totaling the sample size to 72 management staff from all the listed firms. The choice of the departments was because they are departments mostly concerned with dividends and capital. The study used both primary and secondary data. Primary data was obtained from questionnaires. The study obtained primary data on dividend policy, capital structure, corporate governance and timely

rendition of information. Secondary data on dividend policy (EPS), ROA and ROE was collected from annual reports and financial statements of the firms. A linear regression model was used to link the independent variable to the dependent variable as follows:

$$Y = \beta_0 + \beta_1 X_1 + e$$

Where:

Y= Financial performance

X<sub>1</sub>= Dividend policy

β<sub>0</sub> = constant

β<sub>1</sub>= are regression coefficients to be estimated

e= stochastic term

## **FINDINGS AND DISCUSSION**

### **Response Rate**

The number of questionnaires that were administered was 72. A total of 70 questionnaires were properly filled and returned. The results for the response rate are as presented in Table 4.1.

**Table 1: Response Rate**

<b>Response</b>	<b>Frequency</b>	<b>Percent</b>
Returned	70	97.2%
Unreturned	2	2.8%
<b>Total</b>	<b>72</b>	<b>100%</b>

The results in Table 1 indicated an overall successful response rate of 97.2%. According to Mugenda and Mugenda (2003) and also Kothari (2004) a response rate of above 50% is adequate for a descriptive study. Babbie (2004) also asserted that return rates of above 50% are acceptable to analyze and publish, 60% is good, 70% is very good while above 80% is excellent. Based on these assertions from renowned scholars, 97.2% response rate is very good for the study.

### **Demographic Characteristics**

This section consists of information that describes basic characteristics of the respondents such as gender of the respondent, age, level of education and work experience.

### Gender of the respondents

The respondents were asked to indicate their gender. The results are presented in Figure 1.

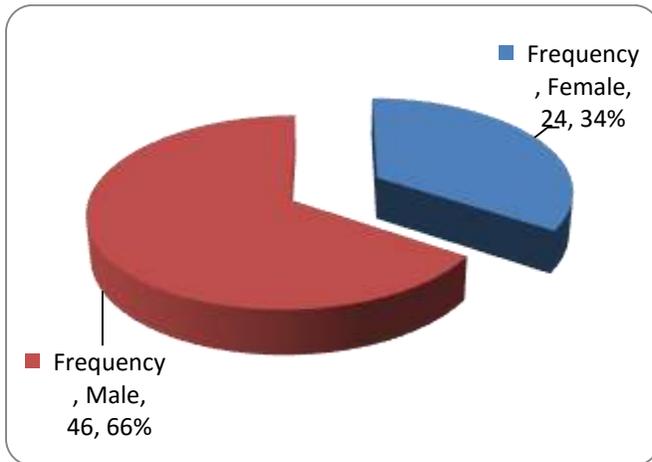


Figure 1: Gender

Results in Figure 1 indicate that majority of the respondents, 66%, indicated that they were males while only 34% were females. This implies that male employees still dominate in these firms listed under Rwanda stock exchange.

### Age

Respondents were also asked to indicate their age brackets. The results are presented in Figure 2.

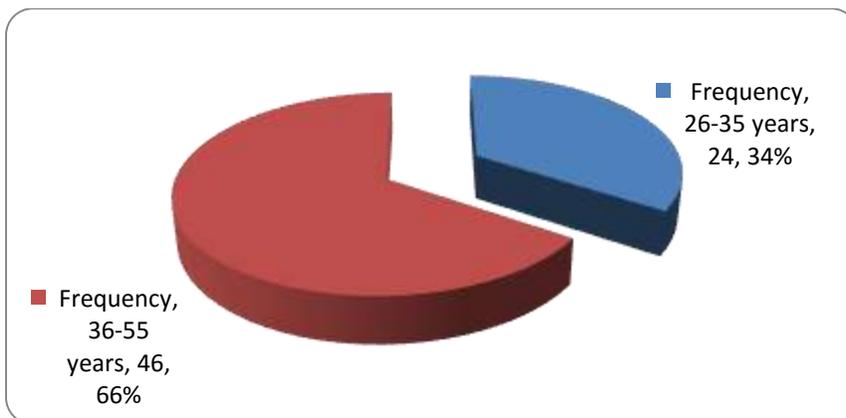
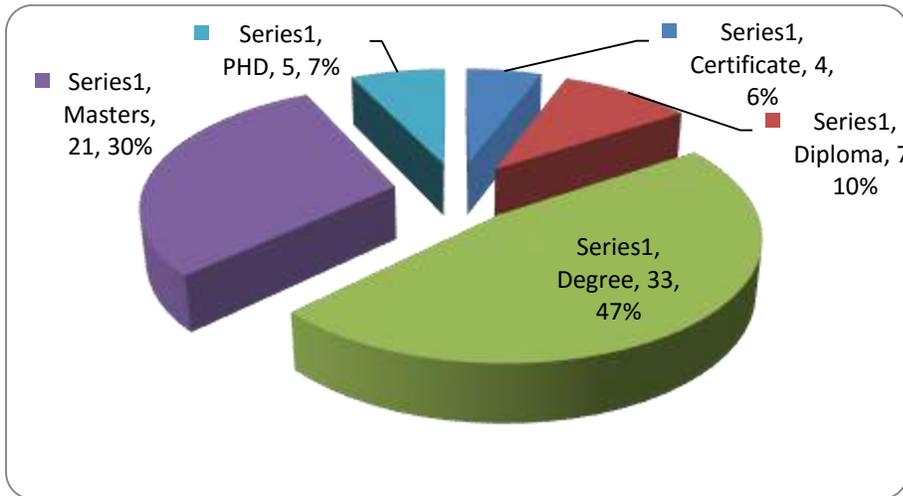


Figure 2: Age Bracket

The results in Figure 2 reveals that majority, (66%), of the respondents were between the ages 36-55years old while 34% were in the age bracket 26-35years.

**Level of Education**

Respondents were asked to indicate their level of education. The results are presented in Figure 3.

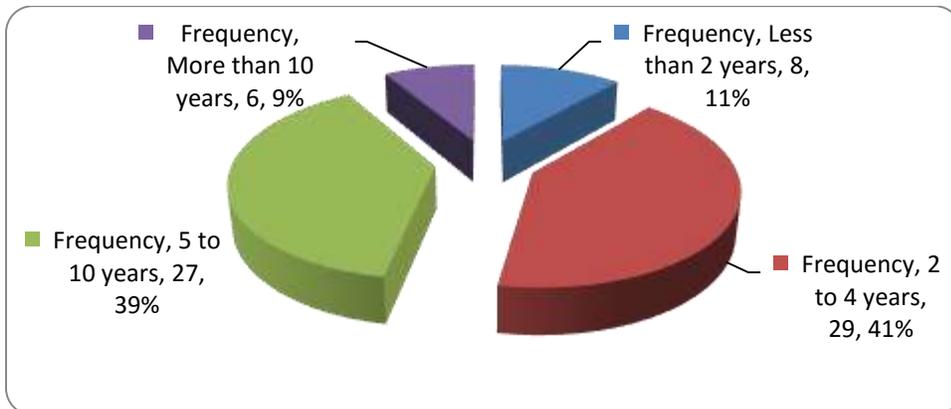


**Figure 3: Level of education**

The study findings indicate that majority, forty seven percent (47%) , of the respondents had Bachelor’s Degree, 30% of the respondents had Master’s Degree. Another 10% had Diploma, 7% had PhD,6% had certificate.

**Work Experience**

The respondents were asked to indicate the duration they have worked in the firms. The results are presented in Figure 4.



**Figure 4: Work experience**

The results in Figure 4 indicates that majority of the respondents who were 41% had worked in these firms for duration 2 to 4years, 39% had worked for 5-10 years, 11%had worked for duration of less than 2 years while only 9% had worked in these firms for more 10 years. This implies that majority of the respondents had not worked in the organization for a long period.

**Correlation Analysis**

The study sought to establish the association among the study variables. The results are as presented in Table 2.

**Table 2: Correlation Analysis**

		Dividend policy	ROA	ROE
Dividend policy	Pearson Correlation	1	.297*	.447**
	Sig. (2-tailed)		0.04	0.001
ROA	Pearson Correlation	.297*	1	.775**
	Sig. (2-tailed)	0.04		0
	N	48	48	48
ROE	Pearson Correlation	.447**	.775**	1
	Sig. (2-tailed)	0.001	0	
	N	48	48	48

The results in Table 4.2 indicate that dividend policy is positively associated with ROA. The results further indicate that the association between dividend policy and ROA is significant at 5% level of significance. The implication of the results is that an increase in dividend policy and corporate governance is associated with an improvement in ROA. The findings agree with the findings of a study by Charles, Joseph and Jane (2014) which indicated that there was a significant positive relationship between dividend policies of organizations and firm’s profitability. Furthermore, the findings agree with findings of a study by Uwalomwa, Jimoh&Anijesushola (2012) which found out that there was a significant positive association between the performance of firms and the dividend payout of the sampled firms in Nigeria.

Furthermore, the findings reveal that dividend policy is positively associated with ROE. The results further indicate that the association between dividend policy and ROE is significant at 5% level of significance. The implication of the results is that an increase in dividend policy is

associated with an improvement in ROE and vice versa. These study findings are consistent with the findings of a study by Adediran&Alade (2013) which indicated that there was a significant positive relationship between dividend policies of organizations and profitability, there was also a significant positive relationship between dividend policy and investments and there was a significant positive relationship between dividend policy and Earnings per Share.

**Descriptive statistics**

The respondents were asked to rate various statements on dividend policy on a likert scale of 1 to 5. The statements were based on a likert scale ranging from strongly disagree rated as 1, disagree rated as 2, neutral rated as 3, agree rated as 4 and strongly agree rated as 5. The results are presented in Table 3.

**Table 3: Attributes of Dividend Policy**

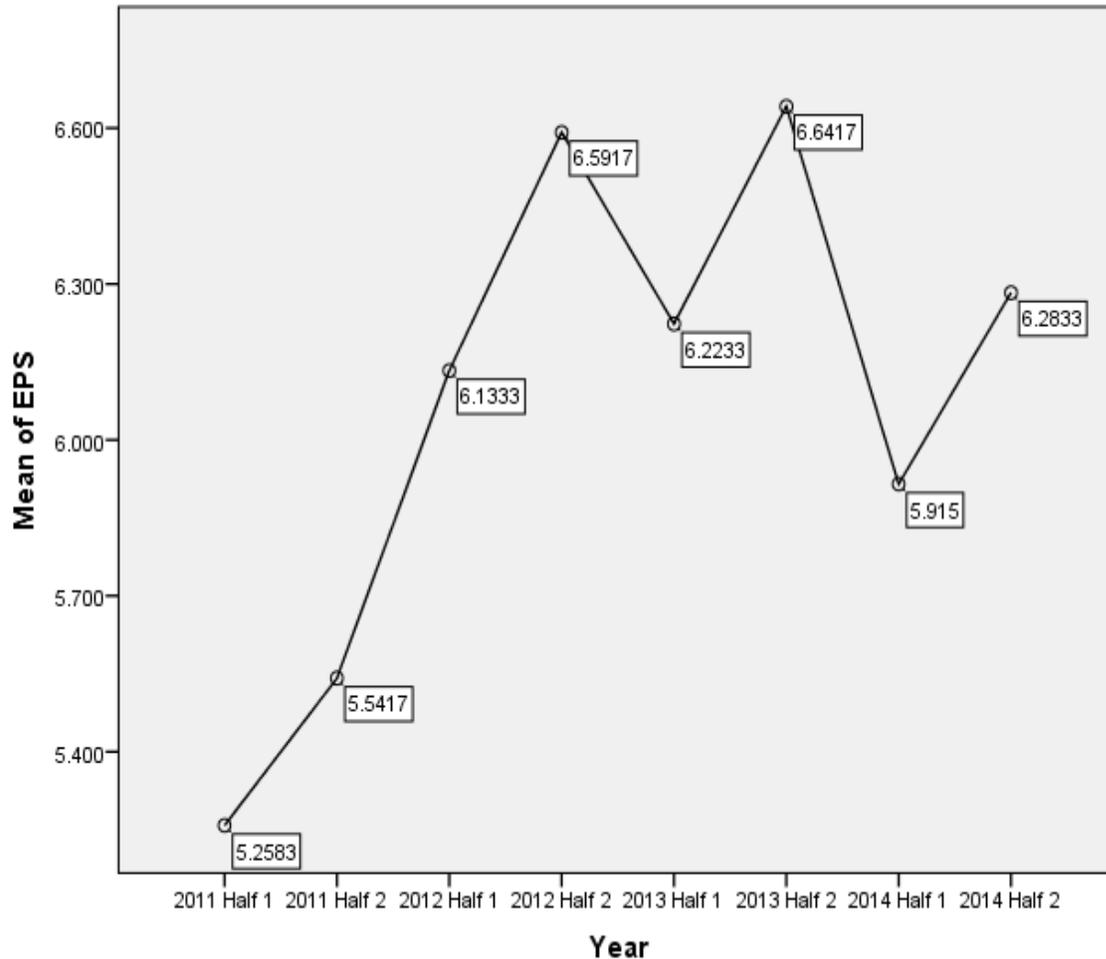
	1	2	3	4	5	Mean	Std Dev
The company operates under established and regularly observed dividend policy	10.00%	7.10%	8.60%	35.70%	38.60%	3.86	1.29
The company pays dividends in correlation with its value	4.30%	2.90%	5.70%	44.30%	42.90%	4.19	0.98
Your company prefers to pay dividends to shareholders than interest to debentures holder because of the incidence on profitability	7.10%	4.30%	4.30%	47.10%	37.10%	4.03	1.12
The shareholders subscribe to high gaining	2.90%	4.30%	5.70%	42.90%	44.30%	4.21	0.95

	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>Mean</b>	<b>Std Dev</b>
Company performs better because of staff share scheme	2.90%	5.70%	7.10%	58.60%	25.70%	3.99	0.91
<b>Average</b>						<b>4.05</b>	<b>1.05</b>

The study findings reveals that on the question on whether the company operates under established and regularly observed dividend policy, majority 74.3% of the respondents agreed. On the issue whether the company pays dividends in correlation with its value, majority 87.2 % affirmed that the company pays dividends in correlation with its value. Another 84.2% of the respondents indicated that the company prefers to pay dividends to shareholders than interest to debentures holder because of the incidence on profitability. Shareholders subscribing to high gaining indicated that majority 87.2% agreed that this influences financial performance. Further, majority 84.3% agreed that the company performs better because of staff share scheme. On a five point scale, the average mean of the responses was 4.05 which means that majority of the respondents were agreeing to the statements in the questionnaire. The standard deviation was 1.05 meaning that the responses were clustered around the mean response.

**Trend Analysis of Dividend Policy**

The study also sought to establish the trends of dividend policy measured in terms of Earning per share. The results are as presented in Figure 5.



**Figure 5: Trend Analysis Dividend Policy**

The results in Figure 4.5 indicates that the mean earnings per share had increasing trends from 5.258 in the first half of the year 2011 up to 6.591 at the end of the year 2012. From the year 2012 the earnings per share was unsteady with increasing and decreasing trends. The mean highest earnings per share was 6.64 which was recorded at the end of the year 2013. The findings of the study are consistent with the findings of a study by Adediran&Alade (2013) which found out that the pattern of corporate dividend policies not only varies over time but also across countries, especially between developed, developing and emerging Capital markets.

#### **Relationship between Dividend Policy and Financial performance**

The study sought to establish the relationship between dividend policy and financial performance of firms listed on the Rwanda Stock Exchange. The measures of financial performance were ROA and ROE. The results for Model Summary are as presented in Table 4.

**Table 4: Dividend Policy and Financial Performance (Model Summary)**

	ROA	ROE
R	.297a	.447a
R Square	.088	.200
Adjusted R Square	.069	.182
Std. Error of the Estimate	.142297	.4094731

The results in Table 4 indicate that the association between dividend policy and both ROA and ROE was positive as indicated by and R of 0.297 and 0.447 respectively. This implies that an increase in dividend policy in terms of earnings per share is associated with an improvement in financial performance of the firms listed at the RSE.

Furthermore, the results indicate that 8.8% and 20.0% of the changes in ROA and ROE respectively is explained by dividend policy as indicated by R square of 0.088 and 0.200 respectively. The findings imply that dividend policy explains a larger change in ROE than in ROA. The fitness of the models was also established and the results are as presented in Table 5.

**Table 5: Dividend Policy and Financial Performance (Model Fitness)**

	ROA	ROE
F	4.466	11.466
Sig.	.040b	.001b

The study findings indicated in Table 5 reveal that the F statistic of both the regression model of dividend policy and ROA as well as ROE of 4.466 and 11.466 respectively was significant at 5% level of significance which means that the two regression models fit well.

Furthermore, the study established the coefficients of the regression between dividend policy and financial performance. The results are as presented in Table 6.

**Table 6: Dividend Policy and Financial Performance (Regression Coefficients)**

		B	Std. Error	t	Sig.
ROA	(Constant)	0.085	0.031	2.739	0.009
	Dividend policy	0.008	0.004	2.113	0.040
ROE	(Constant)	-0.024	0.089	-0.266	0.792
	Dividend policy	0.037	0.011	3.386	0.001

**Models**

$$ROA = 0.085 + 0.008 \text{ Dividend Policy}$$

$$ROE = 0.037 \text{ Dividend policy} - 0.024$$

The results in Table 6 indicate that the relationship between dividend policy and both ROA and ROE is positive as shown by a beta coefficient of 0.008 and 0.037 respectively. Furthermore, the relationships are significant at 5% level of significance as indicated by significance levels of 0.04 and 0.001 respectively. The study findings imply that a unit improvement in dividend policy will lead to 0.008 and 0.037 units improvement in ROA and ROE respectively. The findings are consistent with the argument by Adediran&Alade (2013) that dividend policy affects financial performance of a company because if the value of a company is the function of its dividend payments, dividend policy will affect directly the firm’s cost of capital hence performance. The findings also agree with the argument by Agrawal and Jayaraman (2004) who argued if a firm’s policy is to pay dividend each year end to shareholders, the level of activity in the organization will increase to obtain more income and have excess retained earnings to meet the standard set. This improves the performance. Furthermore, the findings agree with the findings of a study by Samuel & Edward (2010) which found out that banks that pay dividend increase their performance.

**Hypothesis Testing**

The study sought to test the null hypothesis that dividend policy does not affect financial performance of firms listed on the Rwanda Stock Exchange. The hypothesis was tested based on the results of an ordinary least square regression model of dividend policy and ROA. A level of significance less than 0.05 leads to the null hypothesis being rejected while a significance level above 0.05 leads to the null hypothesis not being rejected. The findings in Table 6 indicates a level of significance of 0.040 which leads to the rejection of the null hypothesis hence the dividend policy affects the financial performance of firms listed on the Rwanda Stock Exchange.

## **Conclusion**

Based on the study findings, the study concluded that dividend policy is positively and significantly associated with both ROA and ROE and that dividend policy explains a larger change in ROE than in ROA. Furthermore, the study also concluded that dividend policy is positively and significantly related to both ROA and ROE. In general, dividend policy is positively and significantly related to financial performance of firms listed at the RSE.

## **Recommendations**

The study recommends that firms listed at the RSE should improve their dividend policy as it leads to improved financial performance. The firms should operate under established and regularly observed dividend policy and also pays dividends in correlation with its value.

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