

**IMPACT OF FINANCIAL LEVERAGE ON DIVIDEND POLICY OF LISTED
CONSUMERS GOODS FIRMS IN NIGERIA**

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ABSTRACT

This study examine the impact of leverage on the dividend policy of listed consumers’ goods firms in Nigeria. The study covers a period of ten years from 2007 to 2016. Secondary source of data was used. Panel multiple regression techniques was used to analysis the data. The study made use of ex-post facto research design. Sample of seventeen (17) listed consumers’ goods firms was used. Two formulated research hypotheses were achieved after tested. The findings from this study shows that total debt ratio and long-term debt ratio has negative and significant impact on the dividend policy of listed consumers goods firms in Nigeria. Based on these findings, it therefore, concludes that leverage has significant negative impact on the dividend policy of listed consumers goods firms in Nigeria. It is therefore, recommended that Managers should employ financial leverage in a way that enhances value for their company owners, that is, leading to an increase in returns to equity holders. Debt financing in the financial mix of the firm should be done at the optimal level so as to ensure appropriate utilization of the firms’ assets.

Keywords: leverage, long-term debt, total debt, dividend policy

Introduction

The decision of the firm regarding how much earnings could be paid out as dividend and how much could be retained by the firm is the concern of dividend policy. It determines what proportion of earnings is paid out to shareholders by way of dividends and what proportion is ploughed back in the firm itself for reinvestment purposes. The development of such a policy will be greatly influenced by investment opportunities available to the firm and the value of dividends as against capital gains to the shareholders. Firms can retain its free cash flow, either investing or accumulating it, or pay it out through a dividend or share repurchase. The level of equity retained in the company is affected by the amount of earnings paid out to shareholders, financial managers need to make this decision with caution as it is one the critical decisions in financial management.

Dividend policy has remained one of the most controversial issues in corporate finance since the introduction of irrelevance of dividend policy theory by Modigliani and Miller (MM) in the 1960's when they believed in the world of efficient market where dividend policy does not affect the shareholder's wealth. Over the years, series of academic research has been carried out on firms' dividend policy and these have led to a number of competing theoretical explanations for dividend policy.

A growing number of studies have emerged in examining the determinant of dividend policy across countries. Uwuigbe, Jafaru, and Ajayi, (2012) claimed that conventional factors particularly previous dividend and earnings are the major determinant of dividend policy which could means of firm finance such as leverage, corporate governance, external factors among others. This argument is strongly supported by many scholars without considering the effect of financial leverage on dividend policy. For instance, Brittain (1964) focused on tax structure and dividend policy. Pogue (1971) examined the nature of the relationship between dividend and investment opportunity. Pruitt and Gitman (1991) emphasized on investment and financing decisions as they affect dividend decision in U.S. In Nigeria, Adesola, and Okwong, (2009) covered current earnings, previous dividend, cash flow, investment, net current assets and tax etc. as they affect dividend policy. However, the interaction between financial leverage and dividend policy has received less attention in emerging market such as Nigeria.

Abor (2005) view financial leverage as the amount of debt that an entity uses to buy more assets. Leverage is employed to avoid using too much equity to fund operations. An excessive amount of financial leverage increases the risk of failure, since it becomes more difficult to repay debt and affect the dividend decision of the firms. Financial leverage is a risky approach in a cyclical business, or one in which there are low barriers to entry, since sales and profits are more likely to fluctuate considerably from year to year, increasing the risk of bankruptcy over time (Alkhatib, 2012).

The interaction between financial leverage and dividend policy arises from the agency problems existing between principal and the agent (Jensen & Meckling 1976). The principal is the shareholder who employs the agent that is the management to run the affair of the firms in the interest of the shareholder (Jensen 1986). However, as the firms become bigger

the gap between the shareholders and the management becomes wider, thus creating an agency problem. Agency problems show the divergent of interest between the shareholders and the management.

Manufacturing companies in Nigeria, especially the consumer goods sector, is crucial to the growth and development of Nigerian economy considering its contribution to Gross Domestic Product (Dell'Araccia, Laeven, & Suarez, 2017). The consumer goods sector has a total of twenty eight companies quoted on the Nigerian Stock Exchange with over N17, 536,945,110.80 traded by the sector (NSE, 2014). This level of huge investment will attract diversified nature of investors. However, about six (6) listed consumers goods companies listed on the Nigerian Stock Exchange (NSE) have not paid dividends to their shareholders over the past five years (Nigeria Stock Exchange, 2018). According to information obtained from the NSE, the figure represents 25 per cent of the 28 consumers goods companies listed on the daily official list of the NSE as at March 29, 2017. According to Ajayi and Mougouè, (2017), some believe that company profits are best reinvested back into the company, while others are in support of companies that return profits to shareholders. The former group tend to view such company management as having run out of good ideas for the future of the company and may impact the fortunes of the stock in a climate that has been traditionally sold the message that dividend payout is a measure of progress. He however said not paying dividend for a long period of years showed that the companies might be facing serious financial constraints, adding that it is not good for shareholders to have investments that do not yield dividends.

Furthermore, failure of the companies to pay dividend may be attributed to financial leverage of the firms. Dividends are corporate earnings companies pass on to their shareholders, which can be in the form of cash payments or shares of stock.

Analysing factors that tend to influence dividend payout decisions of listed companies in the consumer goods sector becomes a worthwhile research. From the above scenario, it can be deduced that the impact of leverage on dividend policy cannot be under stated especially when viewed within the context of divergent of interests between principals and their agents.

Over the years, series of academic research has been carried out on firms' dividend policy and these have led to a number of competing theoretical explanations for dividend policy. Despite the various studies covering outstanding issues on dividend payments and policies as well as their relevance to investors within developed markets and in the emerging markets, consensus are yet to be reached on what factors constitute determinant with a definite magnitude. A good number of studies have been conducted in both developed and developing countries in order to identify the effect of leverage on firms' choice of dividend policy, but no consensus has been reached (Qamar, Farooq, Afzal, & Akhtar, 2016).

Dividend policy decision has shown conflicting results among researchers. Some studies have shown that dividend policy is irrelevant Saeedi and Mahmoodi, (2011); Abor, (2005); Lawal, and Edwin, (2014).. While some studies have concluded that the dividend policy is relevant to the growth and development of the firms (Pratheepkanth, 2011; Onaolapo and Kajola, 2010). Ahmed, Sheikh and Wang (2011) found positive relation between size and debt that shows in practice larger firms are deploying more debt. Yet,

other studies have documented a positive relationship Toraman, Kihc, & Reis, 2013; Omorogie and Erah, 2010; Akintoye, 2008).

Furthermore, studies also showed conflicting results on the influence of leverage and previous year dividend on the current year dividend payout. For instance, size has positive and significant effect on dividend payout in Rafique (2012), Malik, Gul, Khan, Rehman and Khan (2013). Musiega, Alala, Musiega, Maokomba, Egessa (2013), Ahmed and Murtaza (2015), Kajola, Desu and Agbanike (2015) concluded that leverage has insignificant effect on the firms dividend policy. However, Kaźmierska-Jóźwiak (2015) noted that it has leverage has negative effect on dividend payout, while King'wara (2015) gave a negative and significant effect. The balance between the retained earnings and dividend payout has been treated as the ideal one to optimize the value of the firm (Soyode, 1975; Oyejide, 1976; Ariyo, 1983). Modigliani and Miller (1961) are of the view that potential investors are not concerned with the dividend payment as it has no effect on the financial value of a firm and its stock where as Black (1976) finds no justification for the payment of cash to the stockholders.

With these mixed and conflicting results, the quest for examining the impact of leverage on the dividend policy has remained a puzzle and empirical study continues. If the issues left unresolved it may compound into agency problem and affect the overall growth and development of listed consumers goods firms in Nigeria. Therefore, there is need for more integrative research to resolve the controversies. Moreover, very few studies only examined the influence of leverage on the dividend policy components of listed consumers goods in Nigeria. It therefore, imperative to conduct a fresh research on the subject matter by looking impact of leverage on the dividend policy of listed consumers goods in Nigeria. In order to address the issues raised above, the following research question would be used to guide the study.

To what extent does long-term debt impact on the dividend payout of listed consumers goods firms in Nigeria?; To what extent does total debt impact on the dividend payout of listed consumers' goods firms in Nigeria?;

The broad objective of this study is to examine the impact of leverage on the dividend policy of listed consumers goods in Nigeria. Specifically, the study seeks to; examine impact of long-term debt on the dividend payout of listed consumers goods firms in Nigeria; examine impact of total debt on the dividend payout of listed consumers goods in firms Nigeria.

The study would be guided with the following research hypotheses formulated in a null form.

H₀₁: Long-term debt has no significant impact on the dividend payout of listed consumers goods firms in Nigeria

H₀₂: Total debt has no significant impact on the dividend payout of listed consumers goods in firms Nigeria

LITERATURE REVIEW

This chapter covers the conceptual, theoretical frameworks and empirical studies conducted on the effect of financial leverage on dividend policy of listed consumers goods firms, which will be broadly reviewed.

Concept of Dividend Policy

Dividend policy refers to the decision to distribute all or part of the company's profit in the form of dividends to the shareholders or plough a proportion of the company profit back to the business (Al-Malkawi, Rafferty & Pillai, 2010). It is the practice usually adopted by the management in making dividend payout decisions or the amount of cash distributed over time to stockholders (Lease, Kose, Avner, Uri & Oded 2000). Dividend policy represents an appropriation of profit to shareholder and guideline for paying certain proportion of earnings to investors as dividends (Marfo-Yiadom et al. 2011). In other words, it accounts for how a firm divides its income between retained earnings and dividend. According to Pandey (1999), dividend policy chosen by a firm should maximize shareholders wealth. Payment of dividend most often are made from the current year's profit and sometimes from the general reserve. Dividends can be in the form of cash, stock, stock split, stock repurchases, and regular dividend payment, among others. Hence dividend policy must be evaluated in relation with investment and financing decision of which depend on good corporate governance. Previous studies have focused extensively unconventional factors that influence dividends policy. Current literature, based on agency theory, stewardship theory and stakeholder theory perspective, suggests that corporate governance would influence dividend policy. However, in this study dividend policy will be proxy using dividend payout ratio. Calculated as: $\text{Dividends/Net Income}$

Concept of Financial Leverage

Nirajini and Priya (2013) define leverage as the way in which an organization is financed a combination of long term capital (ordinary shares and reserves, preference shares, debentures, bank loans, convertible loan stock and so on) and short term liabilities such as a bank overdraft and trade creditors. According to Brockington (1990), described leverage of a firm as the components of its sources of financing, broadly categorized as equity and debt finance. From the definitions given by many previous researchers, the amount of debt that a firm uses to finance its assets is called leverage (Kunga, 2015). A firm with a lot of debt in its capital structure is said to be highly levered. A firm with no debt is said to be unlevered. An increase in financial leverage may bring better returns to some existing shareholders but its risk also increases as it causes financial distress and agency costs (Jensen & Meckling, 1976). Also financial leverage is defined as the relationship between the amount of money that a company or organization owes and the value of the company or organization (Guru & Shanmugam, 1998). For the purpose of this study financial leverage is defined as the degree in which organizations are financed by debt expressed in terms of deposits of all types, borrowing, income tax payables and other liabilities. However, in this study financial leverage would be proxies using ratio of total debt to total asset and long-term debt to total asset.

Review of Related Studies

This section presents a review of relevant empirical evidences on financial leverage and dividend policy. It covers studies in developed, emerging, developing economies. The

important of this section is to review previous studies on the subject matter in order to identify area of convergency and divergency and come up with a valid research gap the present study would filled.

Previous studies that have included leverage have not provided a uniform picture of whether leverage has an impact on the company's dividend payouts or not. Amahalu, Chinyere, Nweze and Okoye, (2016) conducted an investigation in United Kingdom and they found no significant relationship between the leverage and the companies dividend payouts. This is contrary to the study made by Al-Kuwari (2009) who found a strong negative correlation between leverage and the dividend payout ratio. Accordingly, Gustav Hellström and Gairatjon Inagambaev (2012) tested the relationship on the Swedish market. In Nigeria, Okoro, Ezeabasili and Alajekwu (2018) examines the determinants of dividend payout of consumer goods companies listed on the Nigerian Stock Exchange. The study made use of 28 listed consumer goods companies as the population. Purposive sampling technique was used and a sample of nine consumer goods companies for a duration of ten years from 2006 to 2015 was selected. Secondary data were collected from audited financial statements of the companies from the websites of the selected companies. Dividend payout ratio was the dependent variable while the independent variables were market value, profitability, financial leverage, company size and previous year dividend payout. Descriptive statistics and multiple regressions were used. The study found that leverage has negative and insignificant effect on the dividend payout. Hence, findings and conclusion of the study may be faulty. Furthermore, Nwaolisa and Chijindu (2016) effect of financial structure on dividend policy of consumer goods firms quoted in Nigerian Stock Exchange. The results of the analysis divulged that financial structure represented by total debt to total equity ratio and short term debt to total equity ratio, negatively affect dividend policy of consumer goods firms measured by earnings per share and return on equity. The study did not cover recent period.

Okoye, Amahalu, Nweze Chike and Obi (2016), assessed the effect of financial leverage on dividend policy on conglomerates listed on the floor of the Nigerian Stock Exchange (NSE) from 2010 to 31st December, 2015. Nine quoted conglomerates were selected for this study. Panel Data was employed in this study. The researchers made use of Ex-post facto research design in conducting the research. The study made use of secondary data obtained from fact books and annual report and accounts of the selected quoted consumer goods firms in Nigeria as at 31st December 2015. Pearson's coefficient of correlation and Multiple Regression Analysis were the statistical tools used in the study. The results of this study revealed that financial leverage (proxy by short term debt, long term debt and total debt) has statistically significant effect on dividend policy of quoted conglomerates in Nigeria at 5% significance level. The study focused on listed conglomerate firms. Hence, the finding may not be generalized. For instance, Kaźmierska-Jóźwiak (2015) report insignificant positive effect, others suggest that size and dividend payout have positive and significant effect (Malik, Gul, Khan, Rehman & Khan, 2013; Alzomaia & Al-Khadhiri, 2013). However, Nguyen (2015) outrightly reported that leverage has negative effect on dividend. This high level of divergence in empirical studies calls for further investigation. Moreover, the timeframe covered by the present study is most recent than the previous studies. The previous studies lack currency; the most current of the existing studies used time frame that stopped in 2013. The need for currency in empirical evidence makes

the present study exigent. On this premises, the present study investigate impact of leverage on the dividend policy of listed consumers goods firms in Nigeria.

Pecking Order Theory

This theory is explained by asymmetric information between management and outsider investors because it encourages firms to prefer internal finance when funding their investments. This is line with the opinion of Myers (1984) and Myers and Majluf (1984) who suggest that capital structure choice is driven by the magnitude of information asymmetry present between the firm insiders and the outside investors. In brief, this theory suggests that firms consider all the financing methods available and choose the least expensive option. This offers a framework that states that when financing new projects, firms first prefer to use internal equity, second prefer to use debt, and last prefer to use external equity. The pecking order theory predicts that high growth firms, typically with large financing needs, will end up with high debt ratios due to their managers' unwillingness to issue equity. However, Barclay, Smith and Morellec (2006) found that firms with consistently high growth use less debt in their capital structures. According to this explanation of the pecking order theory, it is expected that firms with high liquidity tend to use less debt because they are willing to use internal funds when these are available.

Research Methodology

Research design is defined as a blue print of those procedures, which are adopted by a researcher for testing the relationship between dependent variables and independent variables (Khan, 2008). The study employed correlational research design. The aim of the design is to investigate the relationships between variables and to estimate the effect of independent variable on dependent variable, so as to establish a causal relationship or otherwise among variables.

In other to achieve the research objectives, the study focus on all consumers goods that enjoy first-tier listing on the Nigerian Stock Exchange (NSE). The population of this study consists of the twenty-eight consumers goods firms that are listed on the Nigeria Stock Exchange (NSE) as at 31st December, 2016 (NSE, 2016). A sampling frame can be defined as the set of all the available sample units from which a researcher can choose (Donald & Theresa, 2009). According to Mugenda and Mugenda (2003), the sample frame should contain only the elements of the population which are eligible for selection. The study make used of all the seventeen (17) listed consumers goods on Nigeria Stock Exchange as the sample size. This was due to the availability of the financial information of selected firms on the Nigeria Stock Exchange (NSE). This is envisaged to limit the likely error in generalizing the population. The following filtering was deemed appropriate for properly selecting consumers' goods firms in Nigeria.

Any quoted firms that are not fully listed within the scope of this study was not considered in the work; Any holding company that are listed on the NSE and have their share traded on the first tair market was included provided with the availability of their financial statement; Finally, any quoted banks as at 1st January, 2007 but no more listed as at 31st December, 2016 was not considered in this study.

Thus, these seventeen (17) consumers goods firms form the study sample size. The above cohesive representation will enable the research findings to be generalizable to all the consumer goods companies listed on the Nigeria Stock Exchange. For the purpose of this

study, only secondary method of data collection was utilized. The use of secondary source of data is due to the fact that information on the variables used for conducting the research can only be found in the financial statement of the firms.

Model Specification

To check the relevance of the hypotheses, the research engaged a modified version of the model of Odesa and Ekezie (2015). The study engaged the combination of financial leverage and dividend policy ensuring that (Okoye, Amahalu, Nweze, & Chinyere, 2016). model is therefore modified to determine the association between the dependent variable (dividend policy) and multiple regressors. The study, therefore, established a simple model to direct our analysis. This model is as follows;

$$DPOUT_{it} = \beta_0 + \beta_1 TDR_{it} + \beta_2 LDR_{it} + \beta_3 SDR_{it} + E_{it} \quad -i$$

However, in order to suit best purpose of this study, the model was remodified as follow;

$$DPOUT_{it} = \beta_0 + \beta_1 TDR_{it} + \beta_2 LTD_{it} + E_{it} \quad -ii$$

Where:

β_0 = Constant term (intercept)

β_1 – β_2 = Coefficients to be estimated for firm i in period t.

E_{it} = Error term/unexplained variables for firm i in period t.

DPOUT = Dividend Payout Ratio – indicates percentage of earnings paid to common shareholders of firm i in period t.

TDR = Total Debt – indicates the extent of firm i’s leverage in period t.

LTD = Long term Debt – indicates loans and obligations lasting over one year for firm i in period t.

Measurement of the Variable

This section presents a summary of all the variables measurements, the source of the measurement and the a priori expectation. Table 3.1 is shown below:

Table 3.1

Measure of variables and priori expectation

Variable	Proxy	Type	Measurement	Source
Dvidend Policy	DPOUT	Outcome Variable	Gross dividend pay divided net income	Amidu & Abor, 2006
	LTD	Independent	Long-term Debt divided by total asset	Al-Taani, (2013)
	TDR	Independent	Total Debt divided by total asset	Al-Taani, (2013)

Source: Researcher compilation from the Literature

Result and Analysis

This section covers presentation of data, analysis and interpretation of the results. The result from various diagnostic and specification tests as well as the descriptive statistics computed for the sample firms are discussed under this section.

Descriptive Statistics

Descriptive statistics are presented in the table 2, it shows the mean, standard deviation, minimum and maximum value for both outcome and predictor variables. Descriptive statistics in this study considers important elements such as the mean and standard deviation for the variables used in the study where the interaction of data are described as given thus.

Table 2 Summary of Descriptive Statistics

Variable	Mean	Std. Dev.	Min	Max
dpout	.243167	.086717	.000000	.560921
tdr	.647393	.064874	.051877	.854678
ldr	.146865	.134709	.000567	.577578

Source: Stata Output 2018

The table 2 presents the summary of the descriptive statistics for the parameters used specifically dividend payout (dependent variable), while ratio of total debt to total asset and long-term debt to total assets (independent variables). As can be inferred from the outcome of the result, DPOUT had an average of 0.243167 ranging between a minimum of 0.0000 to a maximum of 0.560921 with associated dispersion value of 0.086717 which implies that DPOUT across the industry is significantly dispersed. This finding further signify that that some of the selected firms failed to pay dividend to their shareholder during the observed period.

Furthermore, the ratio of total debt to total asset (TDR) on the other hand averaged 0.854678 ranging between a minimum of 0.051877 to maximum of 0.854678 with standard deviation of 0.064874 suggesting that TDR is significantly dispersed across the firms of the industry. The high value of the means suggested that the selected firms used more debt that equity and that dispersion either maximum or minimum of 064874 shows that there is low level of variation in the used of the debt financing across the unit.

Also the result in the table 2 revealed that long-term debt to total asset measured as the proportion of the company’s long-term debt to the gross asset revealed an average of 0.146865 for the period, ranging between 0.000567 to 0.577578 as minimum and maximum with standard deviation of 0.134709 suggesting that LDR varies mildly across the cross sectional unit.

Correlation Matrix

The correlation matrix explains the level of relationship between explanatory variables and outcome variable in a regression model. The correlation matrix also serves as a preliminary test for multicollinearity. However, a good regression model should not have high value of correlation between independent variables (Ahmed, 2014). Summary of the correlation result are presented in the table 3

Table 3 Summary of Correlation Matrix

e(V)	tdr	ldr	_cons
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TDR	-0.4289634	I	0.000	Fail to Accept
LDR	-0.0940788	II	0.001	Fail to Accept

Source: Researchers Computation, (2018)

Hypothesis One

H₀₁: Total debt to total assets ratio has no significant impact dividend policy of listed consumers' goods firms in Nigeria

Total debt to total asset ratio as one of the explanatory variable of leverage showed a negative and statistically significant relation with the dividend policy. This is evidenced from the coefficient value of -0.4289634 with the p-value of 0.000 less than 5% significance level. This implies that TDR has a significant impact on the dividend policy of listed consumers' goods firms in Nigeria. However, based on this finding the study fail to accept the null hypothesis that Total debt to total assets ratio has no significant impact on the dividend policy of listed consumers' goods firms in Nigeria. This implies that TDR is one of the significant determinant of dividend policy of listed consumers' goods firms in Nigeria. This finding support dividend irrelevant theorist. This finding implies that as firms employed more debt the amount of dividend payout will decrease over times. The findings was not in line with the work of Ibrahim and Tikeliamie 2016, whose found that TDR has no significant impact on organization dividend policy in Pakistan. Also in the line with the findings of Saeed et al (2013) and akinyemi (2013) who's found that ratio of total debt to total asset have a negative and significant impact on the dividend policy of the firms.

Hypothesis Two

H₀₂: Long-term debt to total assets ratio has no significant impact dividend policy of listed consumers' goods firms in Nigeria

The long-term debt to total asset ratio as one of the explanatory variable of leverage showed a negative and statistically significant relation with the dividend policy. This is evidenced from the coefficient value of -0.0940788 with the p-value of 0.000 less than 5% significance level. This implies that LDR has a significant impact on the dividend policy of listed consumers' goods firms in Nigeria. However, based on this finding the study fail to accept the null hypothesis that long-term debt to total assets ratio has no significant impact on the dividend policy of listed consumers' goods firms in Nigeria. This implies that LDR is one of the significant determinant of dividend policy of listed consumers' goods firms in Nigeria. This findings may be attributed to inability of some firm to take tax advantage of debt financing as well as cost that associated with long-term debt such as interest paid on debt, economic factors, repayment plan among others. The finding is in conformity to the work of Khalaf (2013) whose document that long-term debt has negative and significant relationship with the dividend payout of the firms.

CONCLUSION AND RECOMMENDATIONS

The study examine the impact of leverage on the dividend policy of listed consumers firms in Nigeria. The two research objectives was achieved after tested the formulated research

hypotheses. Findings of this study support dividend irrelevant theories. The findings of this study is in conformity with some previous findings by difference scholars. The study confirms that the traditional capital structure theory is valid. It reaffirms that leverage in both the highly and lowly geared firms is statistically significant and is an important determinants of the dividend policy of listed consumers firms in Nigeria.

This study has examines the impact of leverage on the dividend policy of listed consumers firms in Nigeria. Based on the findings of this study, the following conclusion were reach; Firstly, the study found that total debt to total asset ratio has negative and statistically impact on the dividend payout of the firms in Nigeria. Based on this finding, it conclude that total debt ratio has significant influence on the dividend policy of listed consumers goods firms in Nigeria.

The study found that long-term debt ratio has negative and significant impact on the dividend payout of listed firms in Nigeria. Based on this finding, it therefore conclude that long-term debt ratio has significant negative impact on the dividend policy of listed consumers goods firms in Nigeria. It can therefore infer from the study findings that leverage impact the dividend policy of listed consumers' goods firms in Nigeria.

The study examined impact of leverage on the dividend policy of listed consumers' goods firms in Nigeria. In line with our finding, we strongly recommend that since previous dividend payout enhances chances of current dividend payment, it is expedient that the regulatory authorities monitor companies' dividend policy to prevent companies from paying dividend out from unprofitable business period. A stable policy should be decided to declare the dividend constantly. The total income of the current year should not be distributed among the shareholders as a dividend nor to retain total income as a free cash flow, as this will discourage investors. Managers should employ financial leverage in a way that enhances value for their company owners, that is, leading to an increase in returns to equity holders. Debt financing in the financial mix of the firm should be done at the optimal level so as to ensure appropriate utilization of the firms' assets.

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