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## Theories on Dividend Policy Empirical Research in Joint Stock Companies in Kosovo

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### Abstract

Global experience makes clear the importance of dividend policy as a promoter in large corporations. Corporations are the backbone of the economy as a whole, they are a key source of jobs and certainly the largest taxpayer of an economy. In recent years it appears that most common way of distribution in global corporations is cash dividend. In the market we can also face the companies that do not pay cash dividend, and companies that do not pay dividend at all.

Nowadays in the market economy, corporates consider the decision to pay dividends as a quite relevant, because in this way is known the remaining cash flow for investment back into the corporation and cash flow distributed to shareholders. A stable dividend policy gives positive signal to shareholders and can be seen as positive corporate performance. Therefore, this paper tends to face the policies which can be applied from companies on dividend distribution and the factors which indicates in following a certain policy.

The purpose of this paper is to provide information to stakeholders about the factors which determines dividend policy and its role in today's corporations.

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*“Do you know the only thing that gives me pleasure?  
It's to see my dividends coming in”*

*John D. Rockefeller*

## 1. IMPORTANCE OF DIVIDEND POLICY

Dividend is a payment either in cash or other forms that corporations pay to their own shareholders. They are regarded by shareholders as the return on the investment made in the corporation. The Board of Directors has primary responsibility for drafting the dividend policy and decides whether to pay dividends or not? We raise a very basic question: Why should corporations have a strategic policy for dividend payment? "Players in the market", shareholders and investors do not prefer surprises. If the corporation does not have a stable dividend policy, the corporate shareholders will not have any more interest to keep their capital in such corporations. Consequently, the stock price will fall. When shareholders do not receive the expected return (dividend), they express dissatisfaction by selling shares. Therefore, corporations should pay special attention on dividend policy.

There are a variety of factors that affect dividend policy, but we will mention some of them, have greater impact. Factors that affect dividend policy can be divided into two groups:

- Internal factors
- External factors

External factors, which influence the dividend policy, are tabulated as follows:

**The overall economy** in case of uncertain economic conditions and business, management may decide to retain a significant portion of income in the form of retained earnings, with the aim of creating reserves to absorb future shocks.

In the depression, management can hold a large part of its profits to maintain corporate liquidity position. But in periods of prosperity management may be more liberal and pay more dividends due to greater availability of cash flows.

**Situation on Capital Markets** when there is a stable capital market and there are frequent movements of prices, ie when there are unstable prices, then there is a tendency for management to have a more liberal dividend policy. And vice versa, when we have unstable market situation, when company faces frequent price fluctuations, then the dividend policy would be conservative.

**Legal Restrictions** legal regulations vary from country to country, regulations governing dividend policy. Some legal rules stipulate that dividends can be paid from the profit of the current year or from the profit of last year which is kept as a reserve<sup>†</sup>. The rate of capital consumption is considered a protector of shareholders and creditors, prohibiting the payment of dividends out of capital.

**Contractual restrictions** lenders can sometimes put restrictions on dividend payments to protect their interests (especially when the corporation is experiencing liquidity problems). Suppose made a loan agreement stating that the corporation will not declare any dividends for as long as the liquidity ratio is less than 1:1. Or corporations will not pay more than 20% dividends as long as the loan is not repaid, etc.

**Entries in capital markets**, a large corporation with a steady profit, has certainly easier to access the capital markets and thus can borrow money from the markets. But for small corporations and start-up ventures is difficult to obtain funds from the capital markets, therefore it is necessary to keep profits as retained earnings due to the need for additional funds for various investments.

**Internal factors** affecting the dividend policy are numerous, but mention some of them:

**Shareholders expectations**, though the place dividend rate, it is always in the interest of shareholders. Shareholders expect two types of returns: Capital gains, Dividends:

Cautious investors look for dividends because:

- This reduces the uncertainty (capital gains are uncertain);
- Indications for corporate financial strength
- The need for income: Some invest in stocks in order to receive a regular income to meet their living expenses.

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<sup>†</sup> Ciceri, Beshir & Xhafa, Halit, “Financial Management”, Tiranë,2006, page 621

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