

## **Factors affecting Dividend policy**

Dividend decision is one of the important decisions which are taken by the financial manager in any business firm where distribution and retention of the profit is generally decided. It means that under dividend decision, the company has to decide about the portion of the profit which need to be distributed among shareholders in the form of dividend and the portion which need to be retained for the expansion and the growth of the firm. This dividend decision is generally circulated in the form of the policy which is known as Dividend policy. Thus, Dividend policy goes to explain the distribution and the retention of the profit during the particular period of time. While formulating Dividend policy a financial manager considers a number of things which affect the dividend decision in any business firm. These factors are as follows:

(1) Availability of the profit: Dividend policy is directly affected with the amount of the profit as available with the company. The size and volume of the profit has the direct impact on the dividend decision. If the profit is not available, there is not a question of the distribution and retention of profit but if the profit is very much satisfactory, in such a situation, distribution and retention both will be more.

(2) scope of the growth: If the company has the proposal of expansion and growth, in such a situation, the retention will be more in comparison to distribution. Similarly, if a company has profitable investment opportunities and can reinvest earnings at the higher rate than the shareholders, under this situation, the company may retain larger amount of the earnings and may declare the lower dividend.

(3) Liquidity position : While deciding Dividend policy, the liquidity position needs to be examined by the company. If a company has sufficient liquidity to pay dividend, under this situation, the company may declare higher dividend but if the situation is just reverse, the company may not prefer to pay dividend in cash and at higher rate.

(4) Inflationary situation: Inflation has its own impact on the Dividend policy. In the case of inflation, the profit is over estimated due to over valuation of closing stock and under charge of depreciation in fixed assets as depreciation is charged on historical cost of the fixed assets. Thus, in the case of inflation, retention should be preferred in order to keep the capital intact so that sufficient fund may be available at the time of replacement of the fixed assets in future.

(5) nature and type of the company: If the company is growing company or profitable company where market price of share increases with the decrease in the pay out ratio in such a situation retention will be more but if the company is loss making or a declining company, under this situation, payout ratio will be more.

(6)Composition of the share holding: The composition of the share holding also affects dividend decision .The share holders of closely held company may be interested in taking their return from investment in the form of capital gains rather than in the form of dividend which are subject to higher personal income tax. The directors of such company may decide to pay low dividend but the shareholders of widely held company may be interested in taking higher dividend on regular basis .The directors of such company may decide to pay higher dividend.

(7) stability of income :The rate at which the profit is earned by the company also affects dividend decision. If the earnings are stable, the company may decide the dividend at a constant rate but where the earnings are fluctuating, the rate of dividend may be higher or lower depending on the level of income.

(8)Contractual and legal restrictions: The restrictions on the declaration or retention of earnings may also affect the dividend decision. The company cannot declare dividend or distribute earning beyond the rate as a specified by the law or other statutory provisions.

(9)Access to external sources: The extent of access of the company to external sources of funds also affects dividend decision .If the company has a greater access to external sources for raising funds, under this situation, the company may decide to declare high dividend but if the relationship of the company with the external sources is not good ,in such a situation ,the company has to retain greater profit and prefer to declare low dividend.

(10)Attitude and objectives of the management :If the management is very much interested in the growth and expansion of the business firm which leads greater retention by adopting conservative or growth oriented Dividend policy but if the management does not go for immediate expansion under this situation, it may go with the liberal dividend policy where dividend declaration may be at higher rate.