



EFFECT OF DIVIDEND POLICY ON CAPITAL BUDGETING DECISION IN MANUFACTURING COMPANIES LISTED IN NAIROBI STOCK EXCHANGE

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ABSTRACT

The purpose of this study was to investigate the effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi stock exchange. Explaining why companies pay dividend and some do not pay dividends is still problematic to explain and therefore dividend decision remains controversial. The research design to be employed in this study was descriptive research design inform of a survey. The population of interest of this study comprised of 9 manufacturing companies listed at the Nairobi Securities Exchange (NSE, 2015). Purposive sampling was used to select five respondents in the finance department from each company, thus a sample of 45 respondents. The study collected both secondary and primary data. The study sourced secondary data from the audited financial statements at the companies and internet given all these sources has the data available for this study. A questionnaire was used to collect primary data for this study. The pilot study was conducted and this involved pretesting of the data collection instruments. Content analysis and descriptive analysis was employed. Tables and other graphical presentations as appropriate were used to present the data collected for ease of understanding and analysis. Inferential statistics regressions were done to establish effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange. The study established that investment opportunities do affect capital budgeting decision among manufacturing companies to a great extent and that investment opportunities available to the firm constitute an important component of market value. Thus the study concludes that manufacturing companies that have high investment opportunity set have pursued a low dividend payout policy and hence adopted efficient capital decision techniques. The study revealed that firms with high financial leverage and implied financial risk tend to avoid paying high dividends. The study thus concludes that manufacturing companies with high financial leverage have been more profitable, compared to those their counterparts with a low financial leverage, since they can accommodate risk associated with the use of debt finance. The study draws conclusion that profitable firms have ensured that they maintain their current earnings as high as possible since the ratio dividend payout depends on the current earnings of the firm. The study draws further conclusions that profits making manufacturing firms have more growing opportunities since such firms end up retaining a greater portion of their earnings to finance their expansion projects as against returning these dividends to shareholders.

Key Words: *Dividend Policy, Capital Budgeting, Manufacturing Companies*

INTRODUCTION

The goal of corporate entities is to maximize the value of shareholders' investment in the firm. Managers pursue this goal through their investment and financing decisions. Investment decisions involve selection of positive net present value projects while financing decisions involve selection of a capital structure that would minimize the cost of capital of firm. Apart from the investment and financing decisions, managers need to decide on regular basis whether to payout the earning to shareholders, reducing the agency problem (Amidu and Abor, 2006). However, the question remains whether paying out of earnings would essentially create value for the shareholders or not.

The basic objective of shareholder is to maximize their return and this return may be in the form of dividends or capital gain. Investors' decision regarding the return on investment is affected by dividend policy of the company. Arnold (2008) explains the main objective of dividend policy is to maximize shareholders' wealth by maximizing their purchasing power. So maximizing shareholders' wealth depends on the dividend policy of the company because of this shareholders would satisfy their purchasing and consumption patterns.

Dividend or profit allocation decision is one of the four decision areas in finance. The other three are financing, investment, and working capital management decisions. As noted by Ross, Westfield and Jaffe (2002) companies view the dividend decision as quite important because it determines what funds flow to investors and what funds are retained by the firm for investment. Dividend policy can also provide information to stakeholders concerning the company's performance. Generally, the main purpose of investors when investing their assets is to search for income or the rate of return. Dividend is one of the sources of income

in such circumstances; each company is forced to operate with high efficiency in order to maintain the quality and capability of competing to raise a net income with the best result. Therefore, a company determines dividends policy to look forward the profit gained that will be allocated into two components: dividends and retained earnings.

Nairobi Securities Exchange (NSE)

Every company requires funds to meet its financial obligations. In Kenya, the most common sources of funds that are available to companies are shareholders' equity and debt. An optimal combination of debt and equity increases a company's earnings consequently leading to high dividend payout. Shareholders invest in shares with the hope of receiving income in form of dividends, capital gains or bonus issues. Many companies quoted at the Nairobi Stock Exchange (NSE) however, often pay little or no dividends. It was established in 1954, the Nairobi Securities Exchange NSE (2015) was as a voluntary association of stock brokers with the objective to facilitate mobilization of resources to provide long term capital for financing investments. Through stringent listing requirements the market promotes higher standards of accounting, resource management and transparency in the management of business.

Manufacturing sector's contribution to Gross Domestic Product (GDP) has remained at an average of 10 per cent for more than ten years. However, the Vision 2030 stipulates that the sector should account for 20 per cent of GDP. Achieving this goal requires addressing some underlying constraints that hinder faster growth. These include, high input cost, decline in investment portfolio for some activities, transport infrastructure high cost of credit and stiff competition from imports. (Kenya's

Economic Outlook, 2015). Currently we have a total of eighteen (9) manufacturing firms listed in the Nairobi Securities Exchange.

It involves decision making in investing a company funds in the most viable and beneficial project. Capital budgeting is crucial in the maximization of shareholder value as it depends on the capital budgeting decisions made by the managers. Capital budgeting has been described as the formulation and financing of long-term plans for investment (Olawale et al, 2010).

Statement Of The Problem

Companies listed in NSE pay little or no dividend due to high growth opportunities, investment opportunities, low profits and huge debt financing. Manufacturing companies are faced by technology advances thus lead to plant and machinery obsolescent and wear and tear thus requiring replacement. In the global world there is huge competition thus firms in manufacturing sector are suffering from losses due high production cost. Manufacturing firms are also suffering from foreign exchange losses caused by depreciation of Kenyan shillings and low revenues due to imports of cheap products e.g oxygen and sugar.

Many companies are undergoing financial hardship and even bankruptcy due to wrong capital budgeting decisions being made. Capital budgeting requires huge capital outlay, long term implication and high risk. Companies are facing from high taxes when they decide to pay dividend than opting to retain the funds for investment thus lead to capital gains. High dividend payout is leading to lower retention of funds, low growth opportunity and lower liquidity. This problem is affecting investors, management and public.

Empirical studies done in Kenya have been done different aspect of dividend payout, they includes; John (2013) understanding dividend payout ratio is important, because it can provide clues as to the sustainability of a company's dividend and the potential for it to grow. Dayha (2003) examined the relationship between ownership, dividend policy and leverage and conclude that managers make financial policy tradeoffs to control agency costs in an efficient manner, more recently, researchers have attempted to establish the link between firm dividend policy and investment decision

Njoroge (2001) examined relationship between dividend payout and some financial ratios such as return on assets. Maina (2002) carried out a study to establish whether there exists a relationship between dividend and investment decisions since both compete for internally sourced funds and given that funds obtained by debt are very expensive and not available to all firms. However there is scanty of research on the effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange. It is this basis that the study sought to establish effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange.

Objective of The Study

The general objective of the study was to establish effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange. The study was guided by the following specific research objective; to determine the effects of investment opportunities and leverage on capital budgeting decision among manufacturing companies.

Research Questions

The study sought to answer the following research questions

- i. What are the effects of investment opportunities on capital budgeting decision among manufacturing companies?
- ii. To what extent does leverage affect capital budgeting decision among manufacturing companies?

Scope of the Study

This study was limited to Nairobi Securities Exchange and covered 9 manufacturing companies listed in NSE. There are 9 listed companies on the Nairobi Securities Exchange as at August 2015. The researcher believed that this would provide an adequate population and sample for the study therefore give reliable results and findings.

LITERATURE REVIEW

Theoretical Review

This section reviews the theories that guide the study. These theories include signaling theories, pecking order theory bird in hands and agency theory in relation to our variables.

Signaling Theory

Dividend signaling world as modeled in Bhattacharya (1979). We assume that shareholders have a single-period planning horizon and the manager evidence that information asymmetry positively affects dividend policy has also been documented by the free cash flow theory (e.g., Lang and Litzenberger, 1989). It operates in the best interest of current shareholders. The model is developed in terms of marginal analysis for a new project taken on by the firm. We assume that the manager is better informed than outside investors about the firm's future prospects. Thus the manager is the only agent

informed about the distribution of the new project future cash flow.

He attempts to signal his private information via the commitment of an incremental dividend. Dividends are taxed at the rate while capital gains are not taxed. There is a penalty incurred by shareholders in case of cash flow shortfall to cover the committed dividend. If firms have different investment opportunities and these opportunities are difficult to assess by outside investors, dividends become an imperfect indicator of a firm's future prospects. Firms that pay lower dividends because they decide to invest in positive NPV projects face the risk of being pooled with low-paying firms that do not have valuable growth opportunities. At the same time, deciding not to invest in some positive-NPV projects will leave the firm with more cash available for paying dividends. While the long-term prospects of the firm will be affected, the current share price of the firm will be relatively high. This theory relate to investment opportunities

Pecking Order Theory

The pecking order theory is popularized by Myers and Majluf (1984) where they argue that equity is a less preferred means to raise capital because when managers who are assumed to know better about true condition of the firm than investors issue new equity, investors believe that managers think that the firm is overvalued and managers are taking advantage of this over-valuation. As a result, investors will place a lower value to the new equity issuance. This theory maintains that businesses adhere to a hierarchy of financing sources and prefer internal financing when available, and debt is preferred over equity if external financing is required equity would mean issuing shares which meant 'bringing external ownership' into the company. Thus, the form of debt a firm

chooses can act as a signal of its need for external finance.

Firms prefer internal financing. They adapt their target dividend payout ratios to their investment opportunities, while trying to avoid sudden changes in dividends. Sticky dividend policies, plus unpredictable fluctuations in profits and investment opportunities, mean that internally generated cash flow is sometimes more than capital expenditures and at other times less. If it is more, the firm pays off the debt or invests in marketable securities. If it is less, the firm first draws down its cash balance or sells its marketable securities, rather than reduce dividends. If external financing is required, firms issue the safest security first. That is, they start with debt, then possibly hybrid securities such as convertible bonds, then perhaps equity as a last resort. In addition, issue costs are least for internal funds, low for debt and highest for equity. There is also the negative signaling to the stock market associated with issuing equity, positive signaling associated with debt.

Conceptual Framework

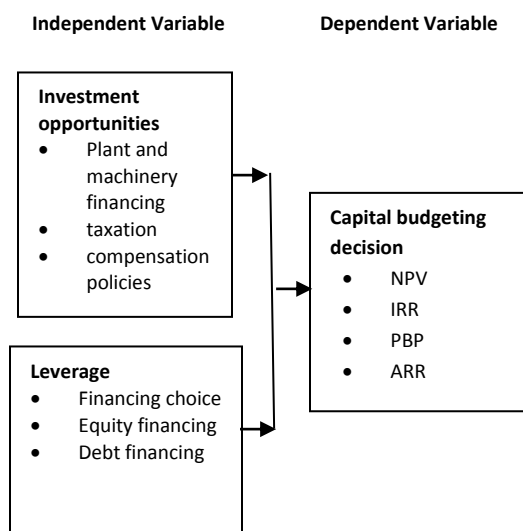


Figure 1: Conceptual Framework

Investment Opportunities

The investment opportunities available to the firm constitute an important component of market value. The investment opportunity set of a firm affects the way the firm is viewed by managers, owners, investors, and creditors (Kallapur and Trombley, 2011). The literature has given considerable attention in recent years to examining the association between investment opportunity set and corporate policy choices, including financing, dividend, and compensation policies (Jones and Sharma, 2011; Abbott, 2011). According to Jones (2011), investment opportunity set represents a firm's investment or growth options but to Myers (2007) its value depends on the discretionary expenditures of managers. He further explains investment opportunity as a yet-to-be realized potentially profitable project that a firm can exploit for economic rents. Thus, this represents the component of the firm's value resulting from options to make future investments (Smith and Watts, 2012).

Kallapur and Trombley (2011) suggest that, the conventional notion of investment opportunity set is of new capital expenditure made to introduce a new product or expand production of an existing product. This may include an option to make expenditure to reduce costs during a corporate restructuring. An investment opportunity has been measured in various ways by various writers. These include market to book value of equity (Chung and Charoenwong, 2009), book to market value of assets (Smith and Watts, 2012), and Tobin's q (Skinner, 2013).

Bhattacharyya and Morrill (2008) find out a negative relationship between managerial compensation and payout based on US data. The Bhattacharyya's model assumes that high

quality managers retain more cash in corporation instead of distributing it to shareholders as dividends in order to invest in positive net present value opportunities while low quality managers distribute more dividends. Comparing managerial contracts, the higher quality managers get higher pay while the lower quality managers get less.

Companies should invest in its personnel in order to increase innovation, efficiency and quality work .it will also reduce employee turnover. Corporate taxes are actual cash outflows and must be accounted for when evaluating a project's desirability. Taxes reduce the expected cash flows and a failure to consider them results in an overestimation of the present value. Abbott (2011) argues that firms that experienced an investment opportunity set expansion (decrease) generally reduced (increase) their dividend payout policy. Others support the fact that firms with higher market-to-book value tend to have good investment opportunities, and would retain more funds to finance such investment, thus recording lower dividend payout ratios (Amidu and Abor, 2006). Riahi-Belkaoui and Picur (2011) also validated the fact that firms in high investment opportunity set group are "PE valued" whilst firms in low investment opportunity set are "dividend yield valued". This implies that for firms in low investment opportunity set, dividends are of greater relevance than earnings whilst the opposite is true for firms in high investment opportunity set. Using market-to-book ratio as proxy for investment opportunity set,

Leverage

The financing choice of firms is perhaps the most researched area in finance in the past decades following the seminal article of

Modigliani and Miller (1958) raising the issue of the relationship between a firms choice of finance and its value. Recently, there are still increasing research and new evidence being sought for the relevance or otherwise of the theory started by Modigliani and Miller. This asserts that firm value is completely independent of how its productive assets are financed. Subsequent researches have suggested a relationship between choice of financing and firm value even though some researchers corroborated the findings of Modigliani and Miller's irrelevance theory (Pruitt and Gitman, 2011). However, studies by Anderson (2013), have proved that in the "real world" market imperfections effectively prohibit the independence of firm's investment and financing decisions.

This market imperfection is primarily coming from the fact that there are taxes, transaction cost, information asymmetry, and bankruptcy cost. This indicates a relationship between the choice of financing and firm value. Financial leverage is said to play an important role in reducing agency costs arising from shareholder-manager conflict and is believed to play a vital role of monitoring managers (Jensen and Meckling, 2006). Farinha (2013) contends that debt is likely to influence dividend decisions because of debt covenants and related restrictions that may be imposed by debtholders. Also, firms with high financial leverage and implied financial risk tend to avoid paying high dividends, so they can accommodate risk associated with the use of debt finance. Easterbrook (2004) and Collins *et al.* (2006) extending the agency theory observe that firms pay dividend and raise capital simultaneously. In the view of Easterbrook (2004), increasing dividends raises the probability that additional capital will have to be raised externally on a periodic basis. This view is

also shared by Green *et al.* (2013) who argue that dividend payout levels are not totally decided after a firm's financing has been made.

Higgins (2012) suggests that firms' dividend payout ratio could be negatively influenced by their need for finance. Thus, dividend decision is taken alongside financing decisions. Higgins (2011) shows a direct link between growth and financing needs, in that rapidly growing firms have external financing need because working capital needs normally exceed the incremental cash flows from new sales. Aivazian and Booth (2013) support the fact that financial constraints can affect dividend decisions, therefore, firms with relatively less debt have greater financial slack and are more likely to pay and maintain their dividends.

Empirical Review

Empirical Studies: Investment Opportunities as Determinant Of Capital Budgeting

Karanja (2013) studied dividend practices of publicly quoted companies in Kenya and established that one of the reasons why firms payout dividends is as a result of lack of investments opportunities which promise adequate returns or more returns than the shareholders would have otherwise received had they been paid dividends for them to make investments independent.

Kinfe (2011) carried out an empirical study on the determinants of dividend payout of banks in Ethiopia. The purpose of the study was to identify the various factors that influence the dividend payout policy of banking firms in Ethiopia during 2006 to 2010 and used the sample of six private banks operating in Ethiopia. The study took dividend Payout Ratio as dependent variable and profitability, liquidity, the effect of previous year's dividend,

leverage, firm size and growth as independent variables. By using the Linter's model, the study concluded that Ethiopian banks more rely upon past dividends to fix their dividend payments. The result also showed the positive relationship between firm size and dividend payout ratio. Also, there was no relationship between payout ratio and profitability, growth and leverage. Furthermore, the study concluded that the firm's liquidity had negative relationship with dividend payout.

The final conclusion of study was that banks in Ethiopia took into account agency conflicts, previous year's dividend and liquidity, more than profitability, leverage and growth when making decision to pay dividends.

Bitok (2004) in a study on the effect of dividend policy on the value of firms quoted at the NSE done for a six year period from 1998 to 2003 established that dividend policy is relevant. They observed that an optimal dividend policy exists. They however put a caveat that the relationship between dividend policy and values of quoted companies at the NSE was weak implying that other factors other than dividend policy like investment and financing decisions affect the value of the firm. Dividend policy in this study was established to be negatively correlated with firm values in line with the tax differential theory.

Empirical Studies: Leverage as Determinant Of Dividend Policy

Dayha (2003) examined the relationship between ownership, dividend policy and leverage and conclude that managers make financial policy tradeoffs to control agency costs in an efficient manner, more recently, researchers have attempted to establish the link between firm dividend policy and investment decision. Following the results obtained by Bradley *et al.*, (1998), firms with high debt ratio would be expected to pay lower dividends.

Leverage is measured using the ratio of total debts to total assets. Since previous studies on capital structure have found debt ratios to be related to many of the right-hand side variables included in the regression model, an instrumental variable is employed to partition leverage into an endogenous part that is attributable to the other explanatory variable, and an exogenous part that is not.

Dong *et al.* (2005) in a questionnaire survey to a panel of Dutch individual investors tested various theories underlying a firm's dividend payout policy. The theories that they examined from an investor's perspective included signaling, agency costs, dividend irrelevance, transaction costs, uncertainty resolution, free cash flow and taxes. They found that respondents strongly believe that dividend payments send a signal about the profitability of the firm. They concluded that firms are justified to keep up dividend payments in good and bad times given the signaling effect of dividends. Their survey results did support pecking order theory while not support for agency theory.

Vasiliou and Eriotis (2003) investigated the association of dividend policy with the debt ratio. The investigation is performed by considering a model that associates the corporate dividend per share at time (t) with a long-run target dividend per share (represented by the dividend variable at time t-i) the earnings per share at time t, and the debt ratio (expressed as the ratio of total debt to total assets) at time t. their regression results suggest that there is a positive association between dividend policy and the examined variables for majority of the firms listed on the Athens Securities Exchange for the period 1996 to 2001.

Pandey (2008) conducted another empirical study examining the industrial trail patterns, trend and volatilities of leverage. The level of

leverage for all industries showed a noticeable increase. The study also indicated that classifying leverage percentages by the type of industry does not produce any patterns which may be regarded as systematic and significant. The trends and volatilities associated with the leverage also did not give any support to the belief and the type of industry impact on degree of leverage.

Critique Of The Literature

The empirical studies which have mainly focused on developed economies show that there is a relationship between the dividend payments and stock prices (Zhou and Ruland, 2006; Pandey, 2004). Maina (2002) carried out a study to establish whether there exists a relationship between dividend and investment decisions since both compete for internally sourced funds and given that funds obtained by debt are very expensive and not available to all firms. Moreover the empirical findings on dividend policy are inconclusive. Existing studies appear to focus on the dividend behaviors of companies in developed economies, but the evidence from developing economies is very limited. Therefore, examining the effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange.

RESEARCH METHODOLOGY

Research Design

The research design that was employed in this study was descriptive research design inform of a survey as its intention of this study is to establish effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange.

Target Population

The population of interest of this study comprised of 9 manufacturing companies listed at the Nairobi Securities Exchange (NSE, 2015).

Sample Size

The study employed a purposive sampling to select one board of directors and four respondents from the Finance department of each company. Through purposive sampling the study selected 45 respondents as the sample size of the study.

Principle Search Tool

The study collected both secondary and primary data. The study sourced secondary data from the audited financial statements at the companies and internet given all these sources have the data available for this study. The secondary data was collected based on the thematic areas of the study. A questionnaire was used to collect primary data for this study. The study used a survey questionnaire administered to each member of the sample population. The questionnaire had both open and close-ended questions.

Data Collection

In order to establish effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange, self-administered questionnaires were distributed among sampled respondents. The questionnaire was designed to establish the effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange.

Data Analysis and Presentation

Before processing the responses, the completed questionnaires were edited for completeness and consistency. A content analysis and

descriptive analysis was employed. The content analysis was used to analyze the respondents' views about the effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange. The data was then coded to enable the responses to be grouped into various categories. Descriptive statistics such as means, median mode and standard deviation was also used to help in data analysis. Tables and other graphical presentations as appropriate were used to present the data collected for ease of understanding and analysis.

Inferential statistics regressions were done to establish effect of dividend policy on capital budgeting decision in manufacturing companies listed in Nairobi Stock Exchange. Data was presented using tables, and pie charts to make them reader friendly. In addition, a multiple regression was used to measure the quantitative data and was analyzed using SPSS too. The regression equation was:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \epsilon$$

Y=capital budgeting

X₁=investment opportunity

X₃=leverage

ε=error term

RESEARCH FINDINGS AND DISCUSSION

Response Rate

The study targeted a sample size of 45 respondents from which 34 filled in and returned the questionnaires making a response rate of 75.6%. This response rate was satisfactory to make conclusions for the study.

Reliability Analysis

A pilot study was carried out to determine reliability of the questionnaires. The pilot study involved the sample respondents among the management staff. Reliability analysis was

subsequently done using Cronbach's Alpha which measured the internal consistency by

establishing if certain item within a scale measures the same construct.

Table 1: Reliability Analysis

Scale	Cronbach's Alpha	Number of Items
Investment Opportunities	0.812	5
Leverage	0.815	5

Gliem and Gliem (2003) established the Alpha value threshold at 0.6, thus forming the study's benchmark. Cronbach Alpha was established for every objective which formed a scale. The study shows that leverage had the highest reliability ($\alpha=0.815$) and then investment opportunities ($\alpha=0.812$).

for between 20 years and above while 20.6% of the respondents had worked for between 0 and 10 years. These findings depict that the respondents had worked for long enough in their organizations to understand them well and thus would give credible information on the effect of dividend policy on capital budgeting decision in their manufacturing companies.

General information

Gender Category

The study requested the respondents to indicate their gender category. From the research findings, the study revealed that majority of the respondents as shown by 58.8% was males whereas 41.2% of the respondents were females. This implies that both genders were fairly engaged in this research and therefore the findings of this research did not suffer from gender bias.

The respondents were requested to indicate their education level. From the study findings, majority of the respondents 64.7% had attained a degree, 23.5% of the respondents had masters while 11.8% of the respondents had attained a college diploma. This is an indication that the respondents were well educated to understand the interview questions.

The respondents were requested to indicate their age category. From the study findings, majority of the respondents were aged between 30 to 39 years as shown by 50%, 23.5% of the respondents were aged between 40 and 49 years, 17.6% of the respondents were aged between 21 and 29 years while 8.8% of the respondents were aged 50 years and above. This is an indication that respondents were picked from all the age categories.

The study sought to determine the respondents' level of management. The findings revealed that most of the respondents were Chief Finance Officer 32.4%, 26.5% of the respondents were Investment Managers, 20.6% of the respondents were Finance Managers, 11.8% of the respondents were the Board of Directors while 8.8% of the respondents were Internal Auditors. These findings depict that respondents were drawn from all the management levels.

The study sought to determine the respondents' length of service in their organization. The findings revealed that majority of the respondents had worked in their organizations for between 10 and 20 years as shown by 55.9%, 23.5% of the respondents had worked

a) Investment Opportunities

The study sought to determine from the respondents the extent to which investment opportunities affect capital budgeting decision among manufacturing companies. From the findings, majority of the respondents indicated the investment opportunities affect capital

budgeting decision among manufacturing companies to a great extent as shown by 64.7%, 26.5% indicated to a very great extent while 8.8% of the respondents indicated to a

moderate extent. These findings show that investment opportunities do affect capital budgeting decision among manufacturing companies to a great extent.

Table 2: Statements relating to Investment Opportunities

Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	Std Deviation
investment opportunities available to the firm constitute an important component of market value	0	2	3	18	11	4.118	0.974
High quality and compensated managers retain more earning in firms in order to invest in project with positive Npv.	2	2	4	18	8	3.824	0.878
Investor considers tax preferences between income and dividends.	0	3	6	16	9	3.912	0.798
firms with high investment opportunity set are likely to pursue a low dividend payout policy, since dividends and investment represent competing potential uses of a firm's cash resources	1	1	5	15	12	4.059	0.885
firms that experienced an investment opportunity set expansion generally reduced their dividend payout policy	1	2	9	19	3	3.618	0.897

The study sought to determine the respondents' level of agreement on some statements relating to effects of investment opportunities on capital budgeting decision among manufacturing companies. The findings revealed that majority of the respondents agreed that investment opportunities available to the firm constitute an important component of market value, as shown by a mean of 4.118; firms with high investment opportunity set are likely to pursue a low dividend payout policy, since dividends and investment represent competing potential uses of a firm's cash resources, as shown by a mean of 4.059; Investor considers tax preferences between income and dividends as shown by a mean of 3.912; High quality and compensated managers retain more earning in firms in order to invest in project with positive Npv. as shown by a mean of 3.824; and that firms that experienced an investment

opportunity set expansion generally reduced their dividend payout policy, as shown by a mean of 3.618. These findings were found to be consistent with those of Karanja (2013) he established that one of the reasons why firms pay out dividends is as a result of lack of investments opportunities which promise adequate returns or more returns than the shareholders would have otherwise received had they been paid dividends for them to make investments independent.

b) Leverage

The study sought to determine from the respondents the extent to which leverage affect capital budgeting decision among manufacturing companies. From the findings, majority of the respondents indicated the leverage affect capital budgeting decision among manufacturing companies to a great

extent as shown by 52.9%, 32.4% indicated to a very great extent while 14.7% of the respondents indicated to a moderate extent.

These findings show that leverage do affect capital budgeting decision among manufacturing companies to a great extent.

Table 3: Statements relating to leverage

Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	Std Deviation
Financial leverage plays an important role in reducing agency costs arising from shareholder-manager conflict	3	1	3	18	9	3.853	0.915
Firms that are large and use internal finances are likely to pay high dividends.	2	3	7	15	7	3.647	0.695
firms with high financial leverage and implied financial risk tend to avoid paying high dividends, so they can accommodate risk associated with the use of debt finance	0	3	5	17	9	3.941	0.847
Demand for high dividend payout by shareholders lead to demand for huge capital thus lead to external financing	1	0	4	15	14	4.206	0.993
High leveraged firms retain more earning to strengthen its equity base.	0	4	8	16	6	3.706	0.730

The study sought to determine the respondents' level of agreement on some statements relating to effects of leverage on capital budgeting decision among manufacturing companies. The findings revealed that majority of the respondents agreed that Demand for high dividend payout by shareholders lead to demand for huge capital thus lead to external, as shown by a mean of 4.206; firms with high financial leverage and implied financial risk tend to avoid paying high dividends, so they can accommodate risk associated with the use of debt finance, as shown by a mean of 3.941; financial leverage plays an important role in reducing agency costs arising from shareholder-manager conflict, as shown by a mean of 3.853; High leveraged firms retain more earning to strengthen its equity base, as shown by a mean of 3.706; and Firms that are large and use

internal finances are likely to pay high dividends, as shown by a mean of 3.647. These findings were found to concur with those of Dayha (2003) examined the relationship between ownership, dividend policy and leverage and conclude that managers make financial policy tradeoffs to control agency costs in an efficient manner. Similarly, Aivazian and Booth (2013) argued that financial constraints can affect dividend decisions; therefore, firms with relatively less debt have greater financial slack and are more likely to pay and maintain their dividends.

c) Capital Budgeting Techniques

The respondents were requested to indicate their preferred capital budgeting techniques. The findings revealed that majority of the

respondents indicated that they prefer the NVP technique as shown by 41.2%, 26.5% of the respondents indicated that they prefer the IRR technique, 23.5% of the respondents indicated that they prefer the PBP technique while 8.8% of the respondents indicated that they prefer the ARR technique. The preference for using the

NPV over using the IRR supports financial theory, which advocates using the superior NPV rather than the IRR technique, as the IRR may give incorrect results in the case where multiple projects being assessed are mutually exclusive (Bennouna, Meredith and Marchant, 2010).

Table 4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.874 ^a	.764	.731	.12225

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings in the table below the value of adjusted R squared was 0.731 an indication that there was variation of 73.1% on the capital budgeting decision due to changes in investment opportunities, and leverage, at 95% confidence interval. This shows

that 73.1 % changes in capital budgeting decision could be accounted to changes in investment opportunities and leverage. R is the correlation coefficient which shows the relationship between the study variables, from the findings shown in the table below there was a strong positive relationship between the study variables as shown by 0.874.

Table 5: ANOVA

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	1.888	2	0.472	3.659	.048 ^b
	Residual	3.741	31	0.129		
	Total	5.629	34			

From the ANOVA statics in the table below, the processed data, which is the population parameters, had a significance level of 4.8% which shows that the data is ideal for making a conclusion on the population parameters as the value of significance (p-value) is less than 5%.

The calculated value was greater than the critical value (2.701<3.659) an indication that there were significant difference between capital budgeting decision and investment opportunities and leverage. The significance value was less than 0.05 indicating that the model was significant.

Table 6: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		

Investment Opportunities	.305	.097	.402	3.144	.020
Leverage	.245	.047	.182	5.213	.001

The established regression equation was

$$Y = 0.878 + 0.305 X_1 + 0.071 X_2$$

From the above regression equation, it was revealed that holding investment opportunities and leverage to a constant zero, capital budgeting decision would stand at 0.878, a unit increase in investment opportunities would lead to increase capital budgeting decision by a factor of 0.305.

A unit increase in leverage would lead to increase in capital budgeting decision by factors of 0.071. The study further revealed that investment opportunities and leverage were statistically significant to affect the capital budgeting decision, as all the p value (sig) were less than 0.05%. The study also found that there was a positive relationship between capital budgeting decision and investment opportunities and leverage.

SUMMARY OF THE FINDINGS

Effects Of Investment Opportunities On Capital Budgeting Decision

The study sought to determine the effects of investment opportunities on capital budgeting decision among manufacturing companies. From the finding the study found out that investment opportunities do affect capital budgeting decision among manufacturing companies to a great extent. The findings revealed that majority of the respondents agreed that investment opportunities available to the firm constitute an important component of market value, firms with high investment opportunity set are likely to pursue a low dividend payout policy, since dividends and

investment represent competing potential uses of a firm's cash resources, Investor considers tax preferences between income and dividends ,High quality and compensated managers retain more earning in firms in order to invest in project with positive Npv and that firms that experienced an investment opportunity set expansion generally reduced their dividend payout policy.

A dividend payment provides cash flow to the shareholders but it reduces firm's resources for investment. Hence, firms should not pay dividend if they have any positive net present value project in hand. If company pays out all the earnings to shareholders, funds for future investment will decrease and dividend may not increase in the future. Moreover, cash dividend is not desirable if investors need to pay taxes on their dividend income

Effect Of Leverage On Capital Budgeting Decision

On the influence of leverage on capital budgeting decision among manufacturing companies, the study revealed that leverage do affect capital budgeting decision among manufacturing companies to a great extent. Majority of the respondents agreed that Demand for high dividend payout by shareholders lead to demand for huge capital thus lead to external, firms with high financial leverage and implied financial risk tend to avoid paying high dividends, so they can accommodate risk associated with the use of debt finance, financial leverage plays an important role in reducing agency costs arising

from shareholder-manager conflict, High leveraged firms retain more earnings to strengthen its equity base and Firms that are large and use internal finances are likely to pay high dividends.

Conclusion

The study established that investment opportunities do affect capital budgeting decision among manufacturing companies to a great extent and that investment opportunities available to the firm constitute an important component of market value. Thus the study concludes that manufacturing companies that have high investment opportunity set have pursued a low dividend payout policy and hence adopted efficient capital decision techniques. Companies need to maximize the value of existing investment opportunity set for future benefits. An investment opportunity gives shareholders capital gains thus taxed less unlike dividend payment which is taxed high. Shareholders preferences also capital budgeting decisions.

The study revealed that firms with high financial leverage and implied financial risk tend to avoid paying high dividends. The study thus concludes that manufacturing companies with high financial leverage have been more profitable, compared to those their counterparts with a low financial leverage, since they can accommodate risk associated with the use of debt finance. Debt finance has interest payment which is tax deductible. Companies can't pay dividends with debt but it can finance its project using debt. Leverage reduces agency cost created by discretionary expense of managers. It reduces manager authority, available cash flow for investment as payment of dividend.

Recommendations

From the study findings, the study recommends. Companies should have good and robust dividend policy. They should enhance their profitability to attract investment in the firm. They should update their shareholders records including next of kin to avoid a deliberate diversion or unclaimed dividend warrants. They should implement more stringent level conditions so as to compel directors to only invest in profitable ventures. Companies that are making losses like Mumias should do a debt restructuring, leadership and governance and a higher brand mix on its product

There is need for the firms to strive towards acquiring external financing because working capital needs normally exceed the incremental cash flows from new sales. This is because financial constraints can affect dividend decisions and firms with less debt have greater financial slack and are more likely to pay and maintain their dividends.

Suggestions For Further Research

The researcher recommends additional research to test and analyze other factors which were not considered like, Impact of age of the firm, previous dividend and tax on dividend payout policy of manufacturing firms. It can also determine dividend payout behavior across sectors of firms listed on NSE. It can also determine investors view on dividend policy by investigating portfolios of various investors e.g. demography so as to unearth the determinants of dividend policy.

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