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IMPACT OF POLITICAL INSTABILITY ON DIVIDEND SUSTAINABILITY OF NON-FINANCIAL FIRM OF PAKISTAN

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IMPACT OF POLITICAL INSTABILITY ON DIVIDEND SUSTAINABILITY OF NON-FINANCIAL FIRM OF PAKISTAN

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Abstract

This research paper aims to identify and discuss the impacts of political instability on dividend sustainability in the non-financial firms of Pakistan. In this study, all non-financial sector businesses listed on the Karachi Stock Exchange will be examined to determine the effect of the dividend strategy on firms performance under moderate or high leverage. This study made use of secondary data from the non-financial sector balance sheet analysis issued by the State Bank of Pakistan to comment on the impacts of political instability and various governments on the dividend policies of the firms in Pakistan.

KEY WORDS:

Political instability, dividend sustainability, Gross domestic (GDP), Company Size

1.0 Introduction

When businesses turn a profit, they have two options: either they keep all of the money for potential future investments, or they distribute some of it as dividends to shareholders. According to the performance of the organization, dividend policy refers to the choice of whether to pay dividends on a consistent basis, at a variable rate, or not at all. The firm's board of directors, who are interested in paying or not paying dividends, made this choice. Depending on the size of the company either small, medium, or large dividend payments to stockholders are given annually, biannually, or monthly. According to Warnes (2014), some occurrences like war, terrorism, and forcible nationalization lead to acute political instability. There are still concerns, such as often changing regulations, unstable currencies, and high levels of corruption, even if these external indicators are not taken into consideration. According to Boone (2007), additional elements such as disparities in legal and regulatory frameworks, the rigidity of the labor market, and unreformed financial systems also constitute significant risk factors. Investors that take on political risk run a greater risk of losing money and of not getting the intended return. Countries with ambiguous government policies may experience this. Compared to financial and financial risk, because political threat is particularly difficult to assess.

Dividend policy, or the payment of dividends, is a crucial subject and one of the corporate finance mysteries that has remained unsolved for more than 60 years. After Modigliani and Miller's (1958, 1961) study on the relationship between dividends and business results, there has been some discussion over the relationship between dividends and firm market prices, as well as whether or not it is relevant at all. However, there is no stability in the link between dividend and share price changes owing to a variety of factors, including investment strategy or dividend distribution based on the boards of directors' choice.

Due to links with politicians, business political approaches provide businesses an informational edge. Political methods shield businesses from unpredictability in future policy. Debt and stock prices rise as a result of political risk. Therefore, it's critical to pinpoint the political characteristics that influence funding costs. Investigating the effects of political risk and corporate political strategy on the cost of debt and equity expenses of non-financial enterprises listed on the Pakistan Stock Exchange is the primary goal of this study (PSX).

Markets and businesses are affected in a variety of ways by government policy. They impose guidelines on how businesses must behave and compete. They control tax and subsidy policies for businesses and have an impact on overall macroeconomic circumstances. The degree of uncertainty in the economy as a whole rises whenever officials dispute more on fiscal, monetary, or regulatory matters. Policymakers, academics, and the general public have all shown a great deal of interest in the consequences that the policy-related uncertainty has on financial and economic activity.

1.1 Background

Political instability has drawn more attention since 2011 in both academic and public policy areas. Changes in national leadership or in government policy can also have political unpredictability effects that interfere with a firm's overall operations and financial results. Political uncertainty peaks around election time when opposing parties are deciding on their economic platforms. Uncertainty influences how businesses behave. Azzimonti (2018) explains that political risk raises legislative dispute and lowers business investment, which raises the cost of financing for businesses. In their study of political vulnerability during races, Julio and Yook (2016) identify the national elections as the primary source of uncertainty.

Additionally, they discovered that business investment decreased during election times, which increased the cost of corporations receiving outside financing. In their research in Brazil, Hillier and Loncan (2019) discovered that political unpredictability raises the barriers for businesses seeking public investment.

Policy uncertainty is the result of government policies and laws that are outside of managers' control, such as terrorist assaults and raw material shocks, making economic policy uncertainty difficult to safeguard, regardless of changes wrought by firm specific source information, technology advancements, but also environment ambiguity. Aside from the timescale allocated for the event driven uncertainty, economic policy uncertainty is linked to being able to run multiple concerns like the financial and political crises, which constitute investor concerns.

According to Huang et al. (2015), we first classify firms as historical non-payers if they haven't paid a dividend in the previous three years in a row before calculating the likelihood that they would stop paying dividends in response to the economic policy uncertainty Similar to this, a company is classified as a dividend payer if it has paid dividends for three years in a row, and researchers look at the chance that these prior dividend payers would continue to do so in reaction to the economic policy uncertainty.

The pecking order hypothesis states that businesses prefer to use internal sources of funding before turning to debt and then equity financing via stock offerings. Larger dividends will be paid out as a result of the businesses having more internal finance due to their increased profitability. As a result, some experts believe dividends to be less significant than capital gains. It is challenging for management to choose an ideal policy since when a corporation develops, shareholders' profits stream likewise expands. Practically every company chooses a dividend

policy that keeps a percentage of net earnings in a way that doesn't jeopardize dividend payments.

1.2 Problem statement

Although there is existing literature on dividend policy, none of it has discussed how uncertainty brought on by governmental laws or rules affects payout policy. Argumentatively, this could be due to difficult measurements of economic policy uncertainty. In general, confusion appears to fluctuate across both short and long periods of time. Recently, Baker et al. (2016) claimed that the ambiguity about monetary, fiscal, and regulatory programs that government policy makers contribute to is what causes economic policy uncertainty, classifying it as a driver of long-term swings in choices. Additionally, Barrero, Bloom, and Wright (2017) provide evidence that the uncertainty around economic policy is related to slower-moving, perhaps more foundational concern sources that are thought to be long-term in nature.

By adopting the Sustainable Development Goals (SDGs) as its own national development plan through an overwhelming National Assembly Resolution in 2016, Pakistan reiterated its dedication to the 2030 Agenda for Sustainable Development. Since then, by incorporating these objectives into national policies and plans, such as the Five-Year Plan, regional growth strategies, and Pakistan's lengthy training vision, the nation has achieved significant progress. A National SDGs Framework was created and adopted in 2018 by the newly elected administration and envisions a strategic strategy to prioritize and localize SDGs.

The resilience of the firm in the face of macroeconomic and microeconomic elements, as well as economic cycles, is a good indicator of company success and business vulnerability. In other words, macroeconomic and microeconomic factors have an impact on the company's performance and hazards. Tax regulations, unique government policies pertaining to certain

firms, foreign currency rates, foreign mortgage rates, foreign economic circumstances, and economic cycles are among the economic variables that can have a direct impact on stock prices and corporate success.

1.3 Research questions

The purpose of this research is to evaluate the following questions.

- There is a relationship between political instability and dividend sustainability?
- How does GDP and size impact on dividend policy?
- What are the factors that impact dividend sustainability?

1.4 Research objectives

The followings are the objectives developed in response to the research questions:

- To determine whether there is a relationship between political instability and dividend sustainability.
- To discuss how changes in GDP have impacted the non-financial firms in Pakistan.
- To understand what are the factors that impact dividend sustainability.

2.0 Literature review

Theoretical background

Nadia Loukil (2020) Findings the government instability positively relative to dividend initiate decision the firm stop to pay dividend and investors also stop to increase their invest. The firms are unwilling to increase their dividend payout ratio and when government leads change the firm decreases their dividend payout. The empirical findings add to the discussion now taking place on the signaling power of dividend policies in developing economies when it is challenging to raise equity capital and controlling shareholders prefer to reinvest profits rather than pay dividends. The investors wait till the new leader shows a new strategy and makes the policy. If the policy is good for investment and boosts the market then investors show interest in the market. In this result control variables GDP and Size do not show a positive effect on the dividend payout ratio.

Political connections refer to interactions between a company's senior executives or any board of directors member and government officials. Businesses form political ties in order to benefit privately and reduce political overall risk. Bondholders are also the ones who stand to gain the most from such tactics. Active corporations find an opportunity to offer efficient ways to manage policy risk, which is also linked to a lower cost of debt for the company. As a result, businesses close to a ruling party can handle greater political uncertainty and have higher loan costs than businesses farther away from the ruling party. It implies that politically engaged businesses profit

from political tactics. The most important factor affecting stock market investment performance is state policy risk.

The bond market receives significant contributions from the insurance and pension fund industries. As they purchase and maintain investments, these organizations are more worried about long-term unpredictability. Policy risk affects the cost of borrowing for businesses. In this sense, the lack of financial flexibility among the enterprises is significantly impacted by local policy uncertainty. These companies' capacity to absorb risk decreases as policy risk increases. According to Bradley et al. (2016), the current interest rate affects investors' risk-return expectations. They also discover that businesses that are situated in a region with significant political power might profit further by supporting the prime minister.

Politically aligned businesses receive greater political favors. Although these alignments offer more benefits and chances for growth, they are also linked to increased degrees of uncertainty for many investors. Bondholders demand a high-risk premium from being exposed to additional uncertainties because political alignment increases the danger of political uncertainty. Businesses without political clout are unable to receive higher rewards. Political unpredictability can alter the capital structure, which can alter business investing practices. Investors continue to be concerned about losing money in nations with unstable political systems. The aforementioned study also looks into whether a nation's naïve political structure benefits investors since it gives them easy access to the legislative branch.

2.1 Factors impacting dividend policy.

In general, uncertainty appears to fluctuate across both short and long periods of time. Recently, Baker et al. (2016) claimed that the uncertainty about monetary, fiscal, and regulatory policies that government officials contribute to is what causes dividend sustainability, classifying it as a

driver of long-term swings in choices. Additionally, Barrero, Bloom, and Wright (2017) provide evidence that long-term uncertainty, is related to slower-moving and perhaps more fundamental uncertainty causes. Other factors that affect uncertainty, such as the volatility of oil prices, CEO turnover, and price fluctuations, are important in determining both short- and long-term uncertainty. Firm long-term decisions, like capital investments, are more vulnerable to long-term uncertainties, such policy shocks based on the news.

The result of governmental regulations and policies that are outside of managers' control, such like; terrorist attacks and raw material shocks, making dividend sustainability difficult to safeguard, regardless of disruption caused by company - specific sources, technology advancements, but also environment ambiguity. Aside from the timescale allocated for the event handling uncertainty, dividend sustainability is linked to event driven uncertainty like the economic and political crises, which composes political uncertainty.

In their analysis, Leroy and Barbara (2008) hypothesized that before- and after-tax capital returns could not be accurately separated from the tax code. They stressed that in order to exhibit the optimum dividend payment behavior, equilibrium concerns and an examination of the impact of taxation on firm value are inextricably linked. Masulis and Trueman (1988) stated that the shareholder considerably prefers to invest in real assets using internal finance as opposed to external because of the delayed personal tax advantage of dividend. Internally financed security investments' profitability is influenced by the security's tax status as well as the shareholder's tax bracket. In contrast, acquisitions of securities using external financing result in a tax loss.

In their study, Nnadi and Apkomi (2008) investigated the impact of taxes on the dividend policies of Nigerian banks and made the argument that several factors affected how corporations distributed their dividends. The banks' dividend policy is to regularly maintain a low but

consistent distribution due to the accessibility of the earnings. The liquidity situation of the corporation is the most crucial element of the dividend structure. A particularly concerning component of a dividend strategy is dividend clients. In their hypothesis, Kose and Williams (1985) connected the signaling equilibrium to taxable dividends. According to their idea, workers of the company who have access to more sensitive information might.

According to Aelee et al. (2011), institutional funds, ownership levels amongst companies, and benchmark to market comparisons are significant factors in equities that pay dividends. According to views on dividend patronage, institutions are drawn to returns for two different reasons. First, because corporations receive a tax benefit from returns, and second, due to restrictions imposed by the "prudent-man rule." In their research, Litzenberger and Ramaswamy (1982) looked at the link between yield on stock and dividends, finding that it is positive but non-linear.

The prophetic rule for predicted dividend yield is free from any information effects that are regulated in dividend yield determinants that forecast the amount of a dividend since it only relies on facts that investors should have access to.

A straightforward model of market equilibrium and an explanation of why businesses that profit from the value of their shares pay dividends were offered by Feldstien and Green in 1983. However, the money may be saved and subsequently distributed to shareholders in a way that would make it easier to classify it as a capital gain. The configuration of shareholders' conflicting preferences in various tax collections and their requirement for portfolio diversification in the elements of uncertainty is what ultimately drives all businesses to pay dividends. Tax-related dividend behaviors influence business investment choices and may contribute to a squandering of the overall investment.

Managers should consider the Linter's (1956) model when deciding on a dividend policy, according to Baker et al. (2001). The management' most important considerations for deciding on dividends were the pattern of previous dividend payments, the strength of profits, and the amount of current and anticipated future income.

In their survey, Baker et al. (1985) described the various kinds of conclusions. According to the initial survey's findings, Linter's 1956 model's key components best described the most significant factors influencing dividends. Results from the second poll indicate that the dividend policy has a significant impact on share value; nevertheless, the most crucial finding is that it is employed to sustain or raise stock price.

Long a contentious and significant subject in financial writing, dividend policy and its factors are. After Lintner's groundbreaking study on dividend continuity in 1956, dividend policy literature underwent ongoing growth, leading to the establishment of two strands of theories: signaling theory (John and Williams, 1985) and market efficiency (Jensen, 1986). The signaling hypothesis is used by researchers to look at the market's reaction to dividend payouts, dividend payment modifications, and their relationship to businesses' potential future profits (Mileti, 2011). In the context of agency theory, scholars have examined the micro- and macro-level drivers of dividend policy, such as management skill, trade - related, listed companies features, and diverse company variables (Mahdzan, Zainudin, and Shahri, 2016).

The influence of uncertainty on dividend policy has acquired widespread recognition among scholars in the present decade and is supported by two associated thrusts. The first one concentrates on uncertainty at the firm level, such as cash flow concern (Chay and Suh, 2009). The second focuses on the effects of firm climate uncertainties brought on by festival activity, such as political turmoil (Huang et al., 2015), concern brought on by the 2008 financial crisis

(Bliss, Cheng, and Denis, 2015), and modifications in tax law (Buchanan et al., 2017). In order to contribute to this expanding base of information, we take a different tack and examine the impact of total economic policy uncertainty on dividend viability using a sample of Pakistan's non-financial listed enterprises from 2000 to 2015.

Changes in economic policy have an influence on financial markets through a number of significant channels, including uncertainty. When there are uncertainties related to potential changes in the macro environment, capital market risk perception rises (Pastor and Veronesi, 2013). The following two factors may have an impact on a company's capacity to continue its dividend payments when risk perception is related with economic policy uncertainty increases. First, during an uncertain time, a rise in managers' riskiness creates an increase in investors' perception of risk, which produces an increase in businesses' capital costs. Increased knowledge imbalance in an uncertain era leads to higher financing costs (Huang et al., 2015).

2.1.1 Impact of political instability on dividend sustainability

Political ties may have an impact on the traditional researcher's perspective on leverage theories. According to the pecking order hypothesis, Myers (1984) posits that businesses favor internal finance over external financing. Contrary to the pecking order idea, it has been discovered that managers favor debt if it is readily available on the market. Political relationships encourage managers to take advantage of possibilities to gain access to funding. Because the majority of managers seem to utilize their financial resources to establish political ties before reaping the rewards in the form of simple access to outside financing (Jensen and Meckling, 1976).

Managers seek future gains through developing personal relationships and using the company's financial resources as a result of their political ties. This aids in gaining influence as a prominent individual with links to the political center. Therefore, the expense of establishing political ties is

considered an agency cost if it aids the firm in obtaining funding. because the managers (agents) carry out their responsibilities on behalf of the company's owners (principals). Getz (1993a) defines agency theory in terms of how parties fulfill their obligations to one another. It concentrates on the difficulty with the principal-agent relationship. The agency theory is used by Getz (2001) to describe the issues that arise between agents and principals in an organization.

Political agents in the government hierarchy, according to Kim, are comparable to other officials and work on their behalf. because they are experts who take away obstacles from businesses' participation in political activities, whether structural or otherwise. Since it is challenging for businesses to influence lawmakers, managers employ a variety of strategies to forge relationships with political power brokers or elected officials. Getz discovers that companies use a variety of strategies to lessen issues brought on by agency connections. As a result, the agency theory aids managers in building relationships with public authorities at the expense of a firm's financial resources. Later, when it lowers the cost of external financing or offers any other economic gain, such linkages or partnerships will be advantageous.

According to Stulz (1988), if debt is simple to get, rising businesses will find it appealing in the early stages of operation. Miller (1977) explains the tax benefit the company received while using debt as an external source of funding by using the trade-off principle.

The advantage of paying interest and tax reduction—the trade-off between interest expenditure, bankruptcy cost, and tax is explained by the trade-off hypothesis. Trade-off theory is crucial in political linkages because corporations profit from easy access to outside financing and tax shelters. When a company has political connections, it may easily get loans and eventually tax advantages. According to Faraji et al. (2020), corporate political ties enable businesses to easily get financing and generate revenue.

According to Harjan et al. (2019), political connections make it simple for businesses to acquire external financing through government-owned banks since politicians have more clout with these institutions. Also discovered by them due to their power and prestige, lawmakers in the ruling party attempt to secure loans from state-owned banks. According to research conducted in Italy by Infante and Piazza (2014), the government-controlled banks there charged various consumers with varied interest rates, which was a reflection of the political clout that the banks were subject to locally. According to Infante and Piazza (2014), businesses with political ties default 50% more frequently than other businesses and receive external financing from banks or other financial entities as a result.

Fisman (2016) draws the conclusion that when governments change, it affects businesses with political clout and easy access to capital. Degryse and Van (2000) examine how businesses and banks interact in terms of preferential access to loans depending on length and scope. They discover that politically linked businesses benefit more from loans from government-owned banks with maturities of three years or longer. Short-term collateral bank loans for politically linked businesses are less advantageous. According to Houston et al. (2014), a change in government has a negative impact for politically linked businesses when it comes to receiving preferential bank loans. According to Chkir et al. (2020), businesses engage in lobbying, make contributions to political campaigns, and maintain relationships with elected officials.

According to Harjan et al. (2019), politically linked businesses benefit from additional subsidies and subsidies, which improves their efficiency and openness.

Considering that politicians have sway over auditing businesses and can choose an auditor who has experience keeping records. so that the quality auditor can call attention to handling errors and so limit the managers' latitude for discretion. Influence prevents the auditor from calling

attention to corporate malfeasance, which improves the reputation of politically linked businesses and inspires market confidence. However, it's possible that the politically linked businesses limit the auditor's authority and contact the following.

2.1.2 Impact of GDP on dividend decision

Previous research indicates that the dividend policy is influenced by the company's success. Companies that do well and make profits will be able to reinvest those gains in the kind of earnings or dividends. The issue of dividend policy is critical because dividend entire data can be employed as a financial system, signaling to outsiders about the company's prospects for growth and stability, and profits play a key role in the financial performance, so the disbursement of dividend payout ratio is an economic decision. The amount of corporate profitability is a key measure of a company's capacity to pay dividends in a particular year. The current and preceding year earnings of the corporation are crucial considerations in determining dividends.

GDP growth rates are the most economically significant indicators, and GDP may also be used to calculate an economy output. Increased GDP increases customer spending power, which causes inflation for the company product. This is a good indicator since the company's revenue will rise as well. As a result, as GDP rises, organizational performance (ROA) rises as well. State Bank of Pakistan’s interest rates will influence commercial bank interest rates. If the interest rates at SBP rise, so will the borrowing costs at commercial banks. The group's plan to address the financing gap, whether by selling stock or bonds, is influenced by SBP borrowing costs.

GDP increases customer spending power, which increases demand for the latest sales. Higher product demand will boost the company's sales. High sales will enhance the company's profitability, and high profitability will impact the amount of profits to be paid. As a result, a rise

in GDP growth relates to dividend payout ratio. Borrowing costs, inflation, the currency rate, and GDP all have a beneficial impact on the dividend policy.

Profitability influences dividend policy since profit is defined as a firm's ability to make profit, and dividends are distributed if the company generates profit. Part of the after-tax profits are given as dividends to shareholders and those who own stock in the firm (retained earnings). If the profit is tiny, the dividend to be distributed is equally little. To ensure that shareholders get high dividends, management will attempt to enhance earnings in order to improve the capacity to pay dividends. The gains supplied to wealthy owners allow stockholders to receive significant dividends.

2.1.3 Impact of corporate governance on dividend policy

The payout policy of the business's dividend behavior throughout any time owing to conflict of interest is determined by firm management and owner conflict. Based on the criteria, management never chooses a dividend policy that does not boost their profit. Instead of distributing dividends, management first chooses to use the remaining profit for the greatest possible investment. Instead of concentrating on enhancing the wealth of the owners, managers frequently use company assets to pursue new narcissistic ideas and perform their own favors. Therefore, poor project allocation and low profitability result in a reduction in dividend payments to investors. According to Freidman, businesses' main goals are to grow wealth and serve the needs of their owners in the greatest possible way.

Many variables influence a company's choice to pay dividends. The political party that rules the country and its duration in office both have an impact on the firm's internal governance and external business policies. (Bliss and Gul, 2012a) contend that it is crucial to recognise the

crucial role that politically linked businesses have played in the growth and success of non-Western economies. In other words, we can comprehend how the influence of political ties in Asian countries causes politically related enterprises to catch the subject's attention (Berkman and Galpoththage, 2016).

Even yet, several companies delisted from stock exchanges because they couldn't grasp these codes when they were really used by PSX listed companies. To address these issues, (CIPE) conducted a meeting in 2006 to determine if the corporation could grasp the codes that had been applied or whether there was a need to alter the laws with clearer explanations (Fudda, 2007). When that moment comes, corporate governance regulations change in 2021, bringing increased levels of responsibility for directors (Awan, 2014). Further enhancing the awareness of the effectiveness of corporate governance compliance is the Pakistan Institute of Corporate Governance (PICG) (Salman and Siddique, 2013).

The adoption of the new corporate governance guidelines in 2002 suggested that the board members should have only yet another directors, never include more than 75% executive directors of the companies, never have an executive member on the internal auditors, and that the chairman of the firm board should preferably be a non-executive director (SECP, 2002). On the other hand, modifications suggest that the system of shared meaning of 2012 required that the board have a lower limit of one non-executive representative from whatever party who has more shares in the company, that the executive directors never be more than 67% of a total size of the board, and that the board's chair and CEO should not be the same.

They also advise that the number of both types of directors may be expanded in accordance with the firm's needs based on the nature of the business, the professional experience of the members, and the need for improved corporate communications. As a result, the interest of directors in

serving shareholders' interests may rise and the authority of executive directors may decline. In order to effectively manage and oversee boards, it is intended to lessen the authority of executive directors and promote independent directors. While the amended CG Code 2012 advocated gender diversity on the boards, the original CG Code 2002 did not specify board diversity (SECP, 2002;2014).

Numerous experts acknowledged the idea that, in the absence of market imperfections, the more profit a corporation generates, the more its value increases before MandM's (1961) study developed the concept. According to the MandM model (1958), under the ideal market hypothesis, the capital structure is immaterial for the financing decision of the business. As a result, internal and external financing are excellent alternatives, and profit has little bearing on the firm's assessment. According to the signaling hypothesis, managers of a company have more access to information about the company's future expectations since they are familiar with many insider reports. They also have a tendency to be aware of whether or not a cash dividend will be paid in the upcoming period, which serves as a signal for him, such as a steady or rising dividend policy.

According to the theory of asymmetric information, shareholders don't have access to enough information about the upcoming payout, which allows management to concentrate on intraday trading when they have superior knowledge. Therefore, as of earning management, the external shareholders are not aware of any such knowledge regarding future predictability to boost share value (Khan, 2016). The relationship between a company's profitability performance, risk management, and corporate governance index is mostly revealed in the financial services sector. Additionally, this is required to lessen how the financial industry perceives it as a "leading

paradigm, assisting firms to identify, analyze, and manage risks at the enterprise level." Adon and Nucu (2020).

2.2 Impacts of dividend policy on non-financial firms

Modigliani and Miller's speculation, regularly known as the profit irrelevance hypothesis, was put out by them (1961). In their article, MM progressed the theory that profit choice has no impact on stock cost nor cost of capital, making it inconsequential for shareholders' wealth. Concurring to Pilotte's (1992) research discoveries, companies that pay out more profits regularly experience slower stock price growth. Agreeing to MM, regardless of how much more the company offers or keeps in order to gather value returns within the form of capital gains, the total of venture profit remains the same. As a result, the financial specialist loses interest. In any case, speculators have the alternative to offer certain offers indeed in case the profits drop short of their expectations.

Two dividend relevance theories developed by Walter (1963) and Gordon (1962, 1963) demonstrate that investors have a favorable opinion of companies that pay dividends to their shareholders. Companies' failure to pay dividends makes them appear more unpredictable to investors, whereas dividend payments boost company share prices.

This hypothesis, proposed by Lintner and Gordon in 1956 and 1959 respectively, contends that investors are always risk-averse and prefer dividends over capital gains in the long run. Therefore, dividend payments significantly affect the share's market price. Investors keep an eye on the firm's dividend policy and weigh payouts against capital gains when making investment selections. According to this belief, a bird in hand is often preferable to a bird in a bush. In this case, the difference between a bird in the hand and a bird in the bush is regarded to constitute a

capital gain. Therefore, receiving money now is preferable to waiting for a future benefit that may or may not include some level of risk. Conversely, dividends are less hazardous than capital. In research they did in Pakistan, Nishat and Irfan (2004) discovered a favorable correlation between dividends with wealth maximization. In Pakistan's stock market, Nazir, Nawaz, Anwar, and Ahmed (2010) investigated the effect of dividend policy on stock return volatility. By choosing a sample size of 73 companies listed on the KSE from the years 2003 to 2008, he used fixed effect model and effect model to panel data. Their study's results revealed a strong correlation between the two factors. In different research, Asghar, Shah, Hamid, and Suleman (2011) assess the impact of dividend distributions on stock prices. By using data from 2005 to 2009, they used non-financial firms from five industries (cement, synthetic fibres, sugar, chemical, and architecture).

Khan (2012) performed second research to ascertain the effect of dividend policy on share prices of Pakistani chemical and pharmaceutical firms. She conducted research showing that cash dividend, retention ratio, and return on equity all strongly positively correlate with stock market values. She said that dividends and earnings per share show a little correlation with stock prices.

In research done in 2012 to ascertain the effect of earnings on profitability and returns, Khan, Zulfiqar, and Shah discovered a weakly positive association between the two variables. Salman (2013) studied the dividend policy in Pakistan's sugar business to see how it affected shareholders' wealth. His findings demonstrated a beneficial relationship between the informative and the dependent variables.

Hasan, Ahmad, Rafiq, and Rehman (2015) performed a second study to investigate the relationship between Pakistan's textile and energy industries' dividend policies and earnings per share. The findings of logarithmic regression demonstrated that the dividend payout ratio had a

detrimental effect on business profitability regardless of industry. A recent research of businesses listed on the Pakistan Stock Exchange was undertaken by Rizwan, Khan, Nadeem, and Abbas (2016). According to their research, the dividend policy has no effect on the return on equity. Another study by Tahir, Sohail, Qayyam, and Mumtaz (2016) examined the impact of dividend policies on business performance and came to the conclusion that there is a positive, statistically significant correlation between firm performance and the dividend payment policies of the individual firms.

Numerous studies demonstrate that the individual transactions of institutional investors directly affect prices. For instance, Keim and Madhavan (1997) examine the transactions for 21 companies over a period of 26 months and discover that investors typically buy stocks at a premium of 0.31 percent and sell them at a discount of 0.34 percent to the previous day's close. 37 investment managers' trades over an 18-month period were examined by Chan and Lakonishok (1995), who found that each deal had both short-term and long-term consequences. Collective institutional trading will likewise have a subsequent price impact, that is, it will mirror the growing effect of the individual institutional investors' trades, if, as the significant relationship with economic growth in these research shows, individual fund managers' trades have a particular price effect.

On the other hand, institutional investors are anticipated to possess greater knowledge than ordinary traders under economies of scale. Institutional trading will affect prices if it provides knowledge to the public (Easley and O'Hara, 1987; Kyle, 1995). According to several empirical studies (see Scholes, 1972; French and Roll, 1986; Barclay, Litzenberger, and Warner, 1990), stock price fluctuations are mostly the result of information disclosed during trade. Since institutional investors are more likely to be knowledgeable than individual investors, if

information that becomes available during trading is the primary driver of stock price fluctuations, collective institutional trading will have a positive impact on returns.

2.4 Impacts of taxes on dividend policy of non-financial firms

A straightforward model of stability point and an explanation of why businesses that profit from the market of their shares pay dividends were offered by Feldstien and Green in 1983. However, the money may be saved and subsequently distributed to shareholders in a way that would make it easier to classify it as a capital gain. In reality, the arrangement of shareholders' conflicting preferences in various government revenues and their requirement for portfolio diversification in the elements of uncertainty is what ultimately drives all businesses to pay dividends. Tax-related dividend behaviors influence business financial decisions and may contribute to a misallocation of the overall investment.

In their study, Azhagaiah and Priya (2008) found that, in general, five factors—sales volume, overall profit development, capital investment choices, capital structure choices, and cost of capital—have an influence on the wealth of shareholders. Typically, a greater dividend raises the share's market value while a smaller payout lowers the share's market value. Due to the owners' privilege of having the present dividend as future revenue, this dividend is seen as a crucial factor in determining the shareholder's total wealth.

Managers should consider the Linter's (1956) model when deciding on a dividend policy, according to Baker et al. (2001). The most important elements are the history of prior dividend payments, the strength of profits, and the magnitude of current and anticipated future earnings.

When listed companies announced increases in their cash dividends and bonus issues in the form of stock dividends, Travlos et al. (2001) looked at how the burgeoning Pakistan stock market reacted. The settings of microstructures, tax establishments, and control conditions of various

markets help to understand the payout dividend policies of the developing stock markets in Pakistan.

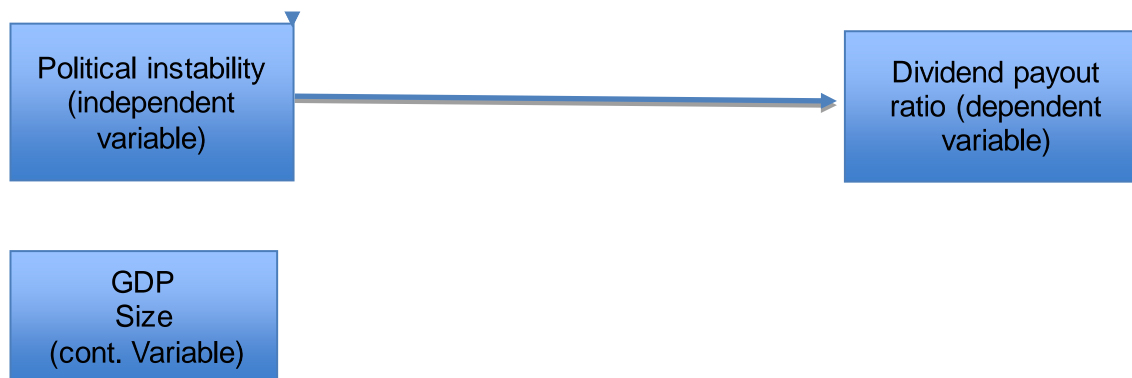
Actually, the cautious effort made by the Cyprus-based listed businesses has a big influence on dividend growth and association of irregularity gaps with investors via their dividend distribution policies.

A favorable link between cash dividends and administrative alternatives was discovered by Wu et al. (2008). It implies that management who has stock options could want to provide cash dividends to drive up the price of the stock.

While many past theories concentrated on non-dividend protected options, this study took into account Taiwan's protected options for dividends, which differ from earlier studies. Employees alter stock option incentives in the wake of stock buyback. Particularly, the businesses undermine the prospect of signaling for firm undervaluation by repurchasing shares to finance options. compiled samples of significant Pakistani corporations that trade on the Karachi Stock Exchange from 2002 to 2008 and discussed the relationship between these companies' dividend policies and corporate leverage.

The first hypothesis is supported by the study's finding that taxation and dividend income are positively correlated. The research also indicates a significant connection between the main and auxiliary factors, supporting the findings of the Nnadi and Apkomi studies (2008). The tax rate plays a significant role in how Pakistani non-financial companies formulate their dividend programmes.

Conceptual Framework



Discussion Hypothesis

H1: Political instability positive effect on dividend payout.

In regression test, it shows significant if the political instability increases the dividend payout also be decreases.

H2: GDP and firm size negative effect on dividend payout.

In regression test, it shows insignificant there is no impact on dividend sustainability. Both GDP and size of firm shows no impact on dividend payout of non-financial firm.

3.0 Methodology

The purpose of this study is to determine the impacts of political instability in Pakistan upon the dividend sustainability of non-financial firms. This section will explain in detail the methodology used to analyze the impact and influence of political risks on dividend policies in Pakistan.

3.1 Research design

The objectives of this research are divided into three categories

Explanatory, exploratory and descriptive research. The qualitative analysis has been used to gather the data and information required to establish the correlation between political instability and dividend sustainability in Pakistan. The purpose of this study was to investigate the impact of changing economic policies due to the constantly changing and unstable political environment of Pakistan upon the business sector, specifically covering the non-financial firms of Pakistan. The methodology adopted for the research was secondary research as it can answer the research questions and put the theories to the test it will also help to create a suitable research design (e.g., identify key variables) and will help to Interpret primary research data to get insights into broad patterns in a market or political category and will help recognize the market environment in response to the political shifts and rapid changes in the GDP.

3.2 Research framework

As the secondary data will be used to compare occurrences over a period of time between different political regimes and during different GDP, therefore it will be ensured to complete the outcome data. The covariates will be determined to conduct the research among which the dependent variable and independent variables will be separated. Literature analysis and data

gathered from the authentic sources will be gathered and arranged to determine the validity of the conduct and the relationship between co-variants. Using a scatter plot, we can generally assess the relationship between the variables and determine whether they are correlated or not. The correlation coefficient is a value that indicates the strength of the relationship between variables. Correlation matrix of theoretical variables will be developed to assess the correlation between the variables such as political instability, dividend policy and non-financial firms of Pakistan.

3.3 Source of data

The principal data has been collected from the secondary sources including the annual reports of Pakistan Stock Exchange (PSX) were evaluated to verify the information and to collect further statistical data to determine and prove the relation between political changes and dividend policy in the country. For this purpose, the reports of the 12 companies past 10 years were studied thoroughly to understand the relationship between the variables.

3.4 Measure

The measure of the variables and research objectives was obtained from the statistical data presented in the research papers and economic surveys published in these research articles as well as the official reports of Pakistan Stock Exchange reports in the form of tables, graphs and charts. These values were incorporated in the data presented in the literature review and the discussion part of this research paper to strengthen the argument with evidence from verified sources. Any data from video sources and from interviews of the finance specialists was recorded and presented in suitable methods either charts, tables or graphs and the sources as well as the name of the interviewees was mentioned to quote the reference and to establish the

authenticity. Each of the values quoted was mentioned precisely, any value that was numerically lengthy was rounded off to the nearest decimal value or a whole number.

3.5 Ethics

Ordinarily, auxiliary information are ones that were gathered for targets other than the current study as part of another investigation project. They might be information collected by government organizations (such as the census, but also increasingly administrative data), information collected by businesses (such as information set of stock costs), or information from past research activities. In spite of the fact that secondary examination of subjective information is more broad, they are more often quantitative. As a result, data was de-identified before being given to the analyst, and it was thought that study participants had given their understanding. Also, the analysis's discoveries avoided members from being re-identified, and the use of the information must not cause hurt or trouble. In order to utilize and analyze the information that was publicly open through the Web, books, and maybe other open sources, consent is verifiably allowed. The original data's provenance was recognised, nevertheless. The study team gave explicit, written consent to the usage of the research information that was a component of another pilot study and indeed the data were not publicly available, other than to the original expert panel, and this consent was included in the application for ethical approval.

3.6 Proposed model

$$Y = \beta° + \beta 1X1_{it} + \beta 2X2_{it} + \beta 3X3_{it} + \varepsilon$$

$$DP = \beta° + \beta 1PI1_{it} + \beta 2GDP2_{it} + \beta 3SIZE3_{it} + \varepsilon$$

Here, the equations beta is coefficient.

β° is constant

β1 is coefficient of political instability.

β2 is coefficient of control variable which is GDP growth.

$\beta3$ is coefficient of control variable which is size.

ε is error term.

4.0 Finding and results.

4.1 Descriptive statistic

Variables	Observations	Mean	Std. deviation	Min	Max
DPayout	120	44.20642	34.18353	0	129
Politicals~y	120	2.77	1.814257	0.9	6.6
GDP	120	4.061	2.089172	-1.33	6.15
Sizelog	120	4.768903	0.5357096	3.512951	5.991702

In descriptive analysis the independent variable is political stability, control variable is Gross domestic product, companies size and dependent variable is dividend payout ratio. Total observations 120, Dividend payout ratio has a mean value of 44.20642 with a standard deviation of 34.18353. standard deviation value is high due to the firm setting the values at time its high at the same time its go to zero. In Political stability mean is 2.77 and standard deviation is 1.814257 small value because values set on country level. Size which are total assets of the company has a mean value of 4.768903 with a standard deviation of 0.5357096.

4.2 Hausman test

Also called model specification test. This test is run on panel data to determine which model will be taken between a fixed effect and a random effects model Based on Hausman criteria, the study seeks to choose a fixed or random effect model.

The table below displays the Hausman test result.

	Fd	**Rd**	**Difference**	**St. Err**
Political~ y	-2.82167	-2.935661	.113985	.6688687
GDP	1.03567 2	1.035056	.000616	.1130008
Sizelog	3.91765	5.707669	-1.790019	10.30342

Prob
>chi2=0.9986

4.3 Correlation analysis

	Dpayout	Pol. instability	GDP	Size
Dpayout	1.0000			
Pol. instability	0.0489	1.0000		
GDP	0.1580	-0.0408	1.0000	
Size	0.2080	-0.1220	-0.0399	1.0000

This table response the correlation matrix. To measure the potency of association between variables, study has used correlation analysis (Fidell 2007). The positivity and negativity of

correlation shows the direct increase relation respectively. Positive correlation indicates that as one variable increases, other variable will likewise increase. Dividend payout is highly correlated with Political instability and positive relation.

4.4 Regression

DPayout	Cofficient	STD.err.	z	P>|z|	[95% conf.]	Intervals
Politicalst~y	2.935661	1.550135	-1.89	0.058	-5.97387	.102547
GDP	1.035056	1.230222	0.84	0.400	-1.376134	3.446247
Sizelog	5.707669	9.883172	0.58	0.564	-13.66299	25.07833
Cons	20.91552	46.41075	0.45	0.652	-70.04778	111.8789

The estimated coefficient of political stability is -2.935661. It shows negative impact which means inversely proportional to dividend payout. If the political instability in a country is high it will affect firms which are approved in tests. Nadia Loukil (2020) Findings the government instability positively relative to dividend initiate decision the firm stop to pay dividend and investors also stop to increase their invest. The firms are unwilling to increase their dividend payout ratio and when government leads change the firm decreases their dividend payout. The empirical findings add to the discussion now taking place on the signaling power of dividend

policies in developing economies when it is challenging to raise equity capital and controlling shareholders prefer to reinvest profits rather than pay dividends. The investors wait till the new leader shows a new strategy and makes the policy. If the policy is good for investment and boosts the market then investors show interest in the market. In this result control variables GDP and Size do not show a positive effect on the dividend payout ratio.

5.0 Conclusion and Recommendations

The study is directed to investigate the effect of political instability on dividend sustainability and the control variable (GDP and Size) effect on dividend sustainability. The data is collected from the Pakistan stock exchange, takes 12 non-financial firms of Pakistan and takes ten-year data from 2012 to 2021.

In the study STATA (**general-purpose statistical software package created in 1985**) approach and the panel information is utilized to examine the relationship between political instability and dividend sustainability. The outcomes are practically as indicated by the past led studies, positive relationship between political instability and dividend sustainability.

This study is done thoroughly utilizing the fundamental analysis approach. The Practitioners and investors can use the findings to decide on their investment portfolio. According to the survey, investors in Pakistan are more sympathetic toward dividend income, making developing an optimum dividend policy a crucial decision for management.

Pakistan's government must address the issues that contribute to political upheaval. The textile industry must address social unrest and its influence on asset returns, as well as how political instability affects CG, DP, and CS. Because private sector development is dependent on political stability, investment from abroad in Pakistan may suffer as a result of political turmoil.

Although the study's aims were met, the study's findings must be evaluated with the underlying research limitations in mind. Only samples from the Industrial Company Sector in one nation were used in this study (Pakistan). As a result, the study's generalizability is restricted.

Future research can duplicate this study in other sectors to improve universality of the results. Future research might include more macroeconomic variables that could impact service quality or revenue, such as price inflation.

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