

ABSTRACT

This study investigates whether dividends have information content, specifically whether dividends provide information to the market about future earnings growth. Due to the fact that, dividends reduce the funds available for investment, many market observers and investors associate high dividend payout with weak future earnings growth. Tests using aggregate market data and company-by-company level data however, contradict this view (for the US financial markets). In this study I have done a company-by-company level analysis for the Indian corporate sector to examine the relationship between payout and future earnings growth. The test results show that high-dividend-payout companies tend to experience strong, not weak, future earnings growth. The results not only hold for a short time horizon of one year but for a medium time horizon of 3 years as well. The results were obtained after controlling for the influence of size, earnings yield, Return on Assets (henceforth ROA), Asset growth and for past earnings growth to take into account mean reversion. The Fama-Macbeth procedure (1973) was used to compute the desired t-statistics. A very large cross section (N) over a time series of 15 years (1996-2011) was used for this investigation.