ABSTRACT

Miller and Modigliani have demonstrated that in perfect capital markets the investment and dividend decisions of a firm are separable. This study attempts to empirically examine the separation principle by applying a MIMIC model to the data of Indian manufacturing firms for 2008-2010. The results indicate that the dividend and investment decisions of individual firms are interrelated and thus reject the M-M hypothesis. The study finds that firm profitability and past investments have a significant and positive impact on the investment decisions while size of the firm has a negative impact. Similarly, firm size has a negative impact on dividend policy while firm profitability has a positive influence. The relationship between investment decisions and the dividend policy has emerged negative and significant and is consistent with the results obtained so far in the Indian context.