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**Consequences of Exits from Political Unions
on Dividend Policy: The Case of Ethiopian Split**

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Abstract

This paper examines the consequences of exits from political unions or the split of countries based on dividend policy decision, taking the Ethiopian split as a practical case, which is considered as a major factor in the increase of political tension with Eritrea especially after the secession, that led to the increase in successive political conflicts and dispute over the past years till now. This paper studies the impacts of political conflicts that have been companied with split to this day especially during the period (2010-2019), using a database of six companies from different sectors, from Ethiopia. The results show that the political conflicts, such as split, have a direct impact on the dividend policy.

Keywords: Dividend Policy; Political Exits; Ethiopian Split; Corporate Financial Policies.

JEL Classification: G30, G32, G34, G35, G38

1. Introduction

There is a significant correlation between politics, economics and the financial policy of any country. Gupta (2018) assures that economics and politics are co-determined, especially with regard to fiscal policy, where politics has a strong influence on the national economy and the fiscal policy of any country¹⁵. Moreover, Osterloh (2010) mentions that a country's political environment can affect its economic performance in several ways²¹.

In recent years, we have witnessed the split of many countries around the world, the most important example of which was the split of South Sudan from Sudan in 2011, and Eritrea's split from Ethiopia in 1993 and recently the UK's exit from the European Union in 2020, which is known as Brexit. Acemoglu and Robinson (2012) mention that "States don't fail overnight. The seeds of their destruction are sown deep within their political institutions¹." Usually, most of the separated states, which

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lived in a state of war and violence, face many challenges such as their inability to fully take advantage of the enormous potential of their society to grow, which makes citizens suffer from social and economic problems.

Many factors affect the financial system and its policies. However, this study deals with the impact of the political conflicts derived from the split between Ethiopia and Eritrea in 1993, which was considered as a major factor in the increase in the political tension between the two parties over the past years, which had a lot of consequences on the corporate finance policy, especially the dividend policy.

The rest of the paper is structured as follows: Chapter 2 describes the problem statement and its reasons and results; Chapter 3 expresses the research question and the aims of the study; then, Chapter 4 describes the research methods, including data and methodology; Chapter 5 shows the results and discussions of the study; Chapter 6 includes the conclusions and limitations.

2. Problem Statement

As for Eritrea's split from Ethiopia, the recent conflict is seen as relating to slices of disputed territories along the thousand kilometre border between the two countries, which were not demarcated correctly, more than a century ago by the Ethiopian Empire and Italy. According to Barry and Gilkes (2005), the origin of the dispute between the two parties was due to the differences between the Eritrean and Ethiopian leadership that started in the eighties. Although they both obtained the support of the same ethnic group, from similar peasant societies, and from Marxist ideology, they differed in their goals and aspirations. Therefore, the Popular Front for the Liberation of Eritrea decided that Eritrea would be liberated from Ethiopian rule as one unified country, despite being made up of nine language groups and two main religions, Islam and Christianity⁴.

However, there are a lot of impacts of the Ethiopian split on the economic and financial policies. According to Devarajan et al. (2001), Ethiopia has entered into a protracted civil war along with a bold program to build a socialist economy. At the beginning of 1990, market-oriented reforms were launched in response to deep economic and political crises⁹. As a result of the civil war and internal conflicts, the local economy deteriorated and was significantly affected, especially after Eritrea's split from Ethiopia in 1993.

In addition, Nyasha et al. (2016) stated that although it is now known that the financial system consists of sectors based on banks, the market and companies, most of the previous studies focused on the relationship between economic growth and financial development in general²⁰. This means that there is a historical relationship between economic growth and financial development, so any change in economic policy, the most important of which is political, may lead to an impact on the financial system that is based in turn on banks and companies.

In this context, many researchers carried out a lot of studies about the dividend policy and its theories. According to Frankfurter and Wood (2002), over the past five decades of this century, corporate dividend policy has gained much attention among economists as it has been the subject of extensive theoretical modelling and empirical

examination. Three schools of thought have emerged over the past century¹³. The first point of view adopts the idea that stock dividends are attractive and have a positive effect on price stocks⁷, Boyte-White (2020); Allen and Rachim (1996)². The second group believes that share prices are negatively correlated to dividend payout¹⁸ as Nguyen et al. (2019) and Asghar et al. (2011) mentioned³. The third block of theories confirms that the dividend policy is not related to the evaluation of the share price⁵, as Baskin (1989) demonstrated.

In this paper, we address the issue of the impact of political exits on the corporate financial policies, especially the dividend policy, taking the Ethiopian split as a practical case, through studying the determinants of the dividend policy during a period of political conflicts between the two parties and noticing the changes resulted from it. While other articles just mention the impact of politics on the economy and financial policies in general.

3. Research Questions / Aims of the Research

A political decision such as exits from political unions or the split of countries often has many implications on the economic and financial policy²¹, Osterloh (2010). However, the question remains, do political decisions affect the corporate finance policy, and to what extent this may affect the firm's dividend policy?

There are many studies that investigate about the impact of the politics on the dividend policies. For example, Lei (2015) addressed how the political uncertainty and political decisions can affect the firm's dividend decisions by mentioning that corporate behaviour is subject to the political environment¹⁷. Moreover, North and Thomas (1973) study many countries that witnessed dramatic changes in recent decades, especially that suffered from civil war and political conflicts. Political uncertainty, such as splits or conflicts, is an important political factor that may influence corporate decision-making, especially the dividend policy¹⁹. In addition, Farooq and Ahmed (2019) study the relation between the politics and dividend policy, and the impacts of political decisions on the pay-out policies where they stated that the corporate dividend policies are linked to the political systems¹¹.

Tested Hypothesis:

There are some authors who consider that politics have a weak impact on corporate financial policy, especially on the dividend policy, as they depend on the principle that these issues are internal issues decided by firms, as it is not possible to determine whether there is a direct impact of politics on the dividend policy or not even in case that there is a limited impact. According to Feltri et al. (2017); Roe & Siegel (2011) until the past two and a half decades, finance researchers did not pay much attention to political economy until the impact of politics on the economy began to emerge¹². At that time, analysts didn't study the impact of politics on the economy, especially the performance of companies and their policies, thinking that there was no close relationship between them²³. Moreover, Faccio (2006) mentions that the impact of political ties depends mostly on the level of economic development of the country, where the impact varies from one country to another¹⁰.

H0: The Ethiopian split has no impact on the dividend policy.

On the other hand, there are many researchers who believe that politics has a direct impact on economic and financial policies, especially the dividend policy. According to Julio & Yook (2012), they assure that a lot of research and debate on the relationship between politics and economic outcomes has a long history. According to them, governmental decisions and national leadership policy have a lot of implications on the behaviour of all companies and financial policy¹⁶. Moreover, Lei et al. (2015) mention that the cash dividend policy is one of the major corporate financial decisions that are influenced by political factors¹⁷. In addition, Frederikslust et al. (2008), mention that the perceived excess of the 1980s produced a major regulation of US financial markets that affects the control market, credit markets, and the market structure. These changes have highlighted the impacts of the political environment on financial policies¹⁴.

H1: The Ethiopian split has a direct impact on the dividend policy.

4. Research Methods

This study depends on financial indicators and variables collected from six companies in Ethiopia from different sectors during the period (2010-2019), which reflect a period of political conflicts and instability between Ethiopia and Eritrea that resulted from the beginning of the split between Ethiopia and Eritrea in 1993 till now, where a regression analysis was applied to analyse and interpret the financial data for the firms, in order to notice the impact of the split and the political conflicts on the corporate financial policies, especially the dividend policy, by noticing how much the political decisions affect the variables and how did they change by addressing the variation in the ratios of the variables during this period.

In order to study the indicators and variables of the dividend policy, it has to be mentioned the determinants of the dividend pay-out that were used in this study, where dividend per share was used as a dependent variable since it is an important metric for the dividend policy, and the independent variables are as follows: leverage, profitability, liquidity and size. Several studies used dividend per share as dependent variable to study the determinants of the dividend policy, such as Bostanci et al. (2018), who analyse the factors that affect the dividend pay-out decisions of the companies⁶. In addition to Chauhan et al. (2019), Porwal & Singh (2018) carried out several studies about the determinants of the dividend policy⁸.

Table 1 shows the variables, symbols and their proxies, which are related to the determinants of the dividend policy for the firms.

Table 1. Variables, symbol, proxies and variable type

| Variable | Symbol | Proxy | Variable Type |
|--------------------|---------------|----------------------------------|----------------------|
| Dividend per Share | DPS | Dividend Paid/Shares Outstanding | Dependent |
| Leverage | LEV | Total Debt/Total Asset | Independent |
| Profitability | PROF | Net Income/Total Asset | Independent |
| Liquidity | LIQ | Current Asset/Current Liability | Independent |
| Size | Sz | Natural Log (Total Assets) | Independent |

This study addresses the firm’s specific determinants of dividend policy for six companies from Ethiopia during the period (2010-2019). We obtained all data from annual reports of the companies from their official websites and some data from scientific websites. Therefore, this sample includes six well-known firms from different sectors such as “Ethiopian Air, NBE, Harar Brewery, SAP, Nestle in Ethiopia, NICE’’. The sample consists of different indicators of dividend policy, of the six firms, over a period of ten years, which makes 60 firm-year observations.

Since we have panel data and time series format which includes both cross section and time dimension, we will adopt regression as econometric analysis. Therefore, the empirical expression of the main model in Table 1 is as in Eq. (1). In this model, *i* corresponds to the number of firms and *t* corresponds to the year.

$$DPS_{it} = \beta_0 + \beta_1 Lev_{it} + \beta_2 Prof_{it} + \beta_3 Liq_{it} + \beta_4 Sz_{it} + \varepsilon_{it} \quad (1)$$

According to the above model, we obtain the following equation, where in Eq. 1 the dependent variable is the dividend per share, where leverage, profitability, liquidity and size are the independent variables, *i* represents each company, *t* represents the year, β_0 represents the constant coefficient, where $\beta_1, \beta_2, \beta_3$ & β_4 represents the coefficients of the independent variables.

5. Findings

After examining the variables, indicators and the regression model, table 2 indicates the descriptive statistics for proxies using the regression analysis in order to understand the consequences of the Ethiopian split and political exits on the corporate financial policies, through analysing the variables of the dividend policy during the period (2010-2019).

Table 2. Descriptive statistics

| | | DPS | Leverage | Profitability | Liquidity | Size |
|------------------------|---------|--------|----------|---------------|-----------|---------|
| N | Valid | 60 | 60 | 60 | 60 | 60 |
| | Missing | 0 | 0 | 0 | 0 | 0 |
| Mean | | 1.4435 | .5103 | .4177 | .9230 | 9.4548 |
| Median | | 1.6100 | .5100 | .4050 | .8800 | 10.3700 |
| Std. Deviation | | .59183 | .09877 | .16736 | .23308 | 1.98912 |
| Skewness | | -.316 | .247 | .361 | .653 | -.257 |
| Std. Error of Skewness | | .309 | .309 | .309 | .309 | .309 |
| Kurtosis | | -1.273 | .345 | -1.033 | -.432 | -1.627 |
| Std. Error of Kurtosis | | .608 | .608 | .608 | .608 | .608 |
| Range | | 1.95 | .47 | .58 | .94 | 6.33 |
| Minimum | | .40 | .29 | .18 | .56 | 6.12 |
| Maximum | | 2.35 | .76 | .76 | 1.50 | 12.45 |

Source: SPSS Software, 2020

The descriptive statistics of table 2 shows that the average of DPS for the firms in Ethiopia was 1.44 per share. The average of the leverage was 51%, where the average of the profitability is around 41.7%. However, the average of liquidity was about 0.92. We also notice that the average size of the companies was 9.45 when measured using the logarithm of the total assets.

After examining the descriptive statistics, next we interpreted the results of the correlations below between the variables over the period (2010-2019).

Table 3. Correlations

| | | DPS | Leverage | Profitability | Liquidity | Size |
|---------------|---------------------|--------|----------|---------------|-----------|--------|
| DPS | Pearson Correlation | 1 | .471** | .559** | -.299* | .720** |
| | Sig. (2-tailed) | | .000 | .000 | .020 | .000 |
| | N | 60 | 60 | 60 | 60 | 60 |
| Leverage | Pearson Correlation | .471** | 1 | .247 | -.319* | .475** |
| | Sig. (2-tailed) | .000 | | .057 | .013 | .000 |
| | N | 60 | 60 | 60 | 60 | 60 |
| Profitability | Pearson Correlation | .559** | .247 | 1 | -.255* | .248 |
| | Sig. (2-tailed) | .000 | .057 | | .050 | .056 |
| | N | 60 | 60 | 60 | 60 | 60 |
| Liquidity | Pearson Correlation | -.299* | -.319* | -.255* | 1 | -.158 |
| | Sig. (2-tailed) | .020 | .013 | .050 | | .228 |
| | N | 60 | 60 | 60 | 60 | 60 |
| Size | Pearson Correlation | .720** | .475** | .248 | -.158 | 1 |
| | Sig. (2-tailed) | .000 | .000 | .056 | .228 | |
| | N | 60 | 60 | 60 | 60 | 60 |

** . Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

In this part, the most important factor is the Pearson correlation, where this factor decides whether if there is a positive or negative relationship between the variables, where the value always between [-1 & +1]. While if the value is zero or near to zero, there is no relationship. If we look at the Pearson correlation, we can notice that variables such as leverage, profitability and size have a positive relationship with DPS. While liquidity has a negative relationship with DPS.

So, if we want to analyse the relationship between the variables, we will find that there is a strong relationship between the variables, whether positive or negative.

Table 4 shows the correlation coefficient between the dependent variable and the independent variables, for equation 1 during the period (2010-2019).

Table 4. The correlation coefficients

| Model | | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|-------|---------------|-----------------------------|------------|---------------------------|--------|------|
| | | B | Std. Error | Beta | | |
| | | 1 | (Constant) | -.759 | | |
| | Leverage | .459 | .538 | .077 | .854 | .397 |
| | Profitability | 1.324 | .284 | .375 | 4.663 | .000 |
| | Liquidity | -.224 | .206 | -.088 | -1.089 | .281 |
| | Size | .172 | .026 | .576 | 6.637 | .000 |

a. Dependent Variable: DPS = Dividend Paid / Shares Outstanding

According to the above table, we can notice that profitability and size have a Sig = 0.000 < 0.05; so, these two variables have the most efficiency on the dependent variable (DPS). After applying the correlation coefficient, we can extract the value of the variables in the model, at the below equation.

According to the correlation model, we will obtain the following equation:

$$\text{Equation (1): } DPS_{it} = -.759 + .459 + 1.324 + (-.224) + .172 + \varepsilon_{it}$$

Table 5 shows the regression analysis results according to the hypothesis.

Table 5. The regression analysis results

| Model | | Sum of Squares | df | Mean Square | F | Sig. |
|-------|------------|----------------|----|-------------|--------|-------------------|
|] | Regression | 14.189 | 4 | 3.547 | 30.127 | .000 ^b |
| | Residual | 6.476 | 55 | .118 | | |
| | Total | 20.665 | 59 | | | |

a. Dependent Variable: DPS= Dividend Paid / Shares Outstanding

b. Predictors: (Constant), Size, Liquidity, Profitability, Leverage

$\alpha = 0.000 < 0.05$ or 5% \rightarrow There is a low probability that H0 is true, so we reject H0; [H0: not significant; H1: significant].

6. Conclusions

This paper examines the impacts of the political conflicts in Ethiopia on the corporate financial policies, especially the dividend policy. The political conflicts and the internal fighting resulted from the split between Ethiopia and Eritrea in 1993 to the present day have had many consequences on the two countries, especially the performance of the companies operating there.

A regression analysis was adopted to study the impact of political conflicts on the dividend policy determinants. Our results show that profitability and size are significant determinants of the DPS while leverage, liquidity are not significantly affecting the DPS. Besides, we found that liquidity is negatively associated with DPS. However, leverage, profitability and size have a positive relationship with DPS.

Finally, it is clear that the impact of the split and the political issues differ from one company to another, and this is the case with regard to the variables of the dividend policy. As the impact of political conflicts varies depending on the variables, this assures that the political issues between Ethiopia and Eritrea have a lot of impact on the corporate financial policy, fact that supports the H1 Hypothesis.

This paper has two main limitations. Firstly, this paper required a lot of time and effort due to the lack of data for many companies. Secondly, the study excludes firms missing data on the variables between years 2010 and 2019.

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