

Moderating Effects of Dividend Policy Consistency and ROA on Firm Performance in M&A

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Abstract

The occurrence of a positive abnormal return is the dream of every investor in dealing with the decisions taken by the company, because it can provide its own benefits for stakeholders. Therefore, what can create positive abnormality around the announcement of company decision-making, especially Merger and Acquisition (M&A) decisions? To reveal several factors that can create positive abnormal returns around M&A announcements, this study aims to determine the effect of dividend-paying firms on short-term M&A performance which is moderated by the consistency of dividend policy and Return on Assets (ROA) and controlled by size. company using multiple linear regression model. The data used in this research comprises companies in Indonesia that conducted M&A during the period 2002-2021. The total number of observations in this study is 150, and the research employs the Ordinary Least Squares (OLS) technique for analysis. The results of this study indicate that dividend-paying firm has a significant positive effect on short-term M&A performance. The consistency of dividend policy cannot strengthen the positive relationship between dividend-paying firms and short-term M&A performance, but the firm's performance as reflected in ROA, strengthen the positive effect of dividend-paying firms on short-term M&A performance.

Keywords: Consistency of dividend policy, Dividend-paying firm, Return on assets (ROA), Short-term M&A performance

Introduction

Shareholders primarily invest in companies with the goal of increasing their wealth. It is the company's responsibility to achieve these shareholder goals, one of which is to enhance company performance through Mergers and Acquisitions (M&A) (Brigham & Houston, 2013). A merger involves the legal consolidation of one or more companies with another, resulting in the dissolution of the merging companies by law. An acquisition, on the other hand, is the takeover of ownership or operational control by one company of another (Maheka, 2008). Mergers and acquisitions are strategies that companies can implement to expand operations, enter international markets, improve product lines, and create new entities. Additionally, according to Brigham & Houston (2013), Mergers and Acquisitions (M&A) activities are driven by several motives, including synergy and strategic considerations.

Abnormal returns may result from the announcements of mergers and acquisitions by a company. Positive abnormal returns around such announcements can indicate the success of a company's short-term Mergers and Acquisitions (M&A) performance. The performance of short-term M&A can be assessed by calculating the Cumulative Abnormal Return (CAR) around the announcement (Zhou et al., 2019). The success of short-term Mergers and Acquisitions (M&A) performance, as reflected by a high CAR surrounding the announcement,

is closely linked to the market's reaction. The market tends to react positively when dividend-paying acquirers make such announcements (Glambosky et al., 2020; Sun & Yung, 2022). Dividend-paying acquirers demonstrate disciplined management in paying dividends to shareholders and can prevent managers from pursuing excessive gains that may harm shareholders. These acquirers typically seek targets that can contribute to free cash flow, helping to maintain their dividend-paying capability. This study is grounded in several theories, including life cycle theory, signaling theory, and agency theory.

Life cycle theory suggests that large companies with limited investment opportunities tend to maintain higher levels of free cash flow, which is then used to pay dividends rather than reinvested (De Angelo et al., 2006; Gizelle et al., 2013; Subba et al., 2015; Singh & Elango, 2023). However, shareholders are encouraged to continue seeking investment opportunities, including mergers and acquisitions. Managers of dividend-paying acquirers generally avoid decisions that could undermine the value of Mergers and Acquisitions (M&A) activities, which could negatively affect dividend payments. Companies adhering to life cycle theory consistently strive to maintain their dividend policies and continue paying dividends to shareholders (Glambosky et al., 2020; Zhang & Li, 2021).

Signaling theory suggests that managers, who possess more private information than shareholders, use company actions—such as dividend payments, share repurchases, and takeovers—to communicate their perspectives to shareholders (Dewasiri et al., 2019). According to signaling theory, M&A activities carried out by dividend-paying firms send a positive managerial signal, indicating anticipated synergies from the combination of companies following mergers and acquisitions (Glambosky, 2020; Li & Zhang, 2023). Furthermore, the decision to pay dividends serves as a positive information signal, increasing shareholder confidence in the company's future after a merger or acquisition.

Agency theory, as articulated by Jensen (1986), posits that companies with excess free cash flow are inclined to spend it on mergers and acquisitions, potentially maximizing managerial benefits at the expense of shareholders. Consistent with the bird-in-the-hand theory, shareholders generally prefer that companies distribute excess free cash flow as dividends (Lintner, 1956; Gordon, 1959). Previous research on dividend policies and agency cost theory supports the idea that dividends can create a management discipline mechanism within a company (Claudiu & Marilen, 2014; Baker & Sujata, 2015; Subba & Dollery, 2015). These theories suggest that when a dividend-paying firm announces an M&A, the market reacts more favorably compared to announcements by non-dividend-paying firms, leading to better short-term M&A performance (Glambosky et al., 2020).

The positive relationship between dividend-paying firms and short-term Mergers and Acquisitions (M&A) performance can be further strengthened if the firm has a consistent dividend policy (Glambosky et al., 2020). The market responds more favorably when the firm has a history of consistent dividend payments, as this consistency implies that post Mergers and Acquisitions (M&A) synergies will result in higher profits without compromising the firm's commitment to paying dividends.

Additionally, the positive impact of dividend-paying firms on short-term Mergers and Acquisitions (M&A) performance can be enhanced by the firm's Return on Assets (ROA) at the end of the year preceding the Mergers and Acquisitions (M&A) announcement. A higher ROA indicates better company performance in generating returns on assets, which, in turn, leads to a more favorable market reaction to Mergers and Acquisitions (M&A) announcements by dividend-paying firms.

Research on the relationship between dividend-paying firms and short-term Mergers and Acquisitions (M&A) performance in Indonesia remains limited. This study aims to examine the effect of dividend-paying firms on short-term Mergers and Acquisitions (M&A)

performance, with a focus on the moderating roles of dividend policy consistency and Return on Assets (ROA).

Literature Review and Hypotheses

Mergers and Acquisitions

An acquisition refers to the process of taking control over another company's capital, typically through the purchase of a majority stake (Aprilita et al., 2013). In contrast, a merger involves the unification of two or more companies, where only one entity survives as a legal entity, while the others cease operations (Moin, 2003). Companies engage in Mergers and Acquisitions (M&A) with the primary goal of improving their financial performance (Brigham & Houston, 2013). This decision is often motivated by factors such as synergy and diversification (Gaughan, 2013).

Synergy, in the context of Mergers and Acquisitions (M&A), refers to the interaction between businesses that generates greater profits than each could achieve independently. Experts like Deardorff & Williams (2006) describe synergy as a process where the combined effect of two or more agents exceeds the sum of their individual effects, expressed mathematically as $1+1 > 2$.

Diversification, as explained by Kotler (2000), is a strategy companies use to improve business performance by identifying opportunities to expand their business lines. Companies pursue mergers and acquisitions to achieve diversification, which offers several benefits, including reducing business risks, lowering operational and administrative costs, and enhancing profit stability.

Dividend-Paying Firms and Performance of Short-Term M&A

The performance of short-term M&A reflects the company's future prospects as perceived by investors, which is often indicated by the market's response to the Mergers and Acquisitions (M&A) announcement. A positive market response can lead to abnormal returns, which are seen when the synergy created by the merger or acquisition results in a combined value greater than the sum of the individual companies (Ansoff, 1968).

Dividend-paying firms serve as a mechanism for company discipline, attracting shareholders due to their consistent dividend payments (Glabosky et al., 2020). When such firms announce an Mergers and Acquisitions (M&A), the market typically responds more favorably compared to non-dividend-paying firms. Previous research has identified both debt payments and dividend policies as reflections of company discipline (Myers, 1977; Hennessy, 2004; Diamond & He, 2014; Baker & Sujata, 2015; Claudiu & Marilen, 2014; Subba & Dollery, 2015; Glambosky et al., 2020).

While some studies, like Turki & Dereeper (2017), find no effect of dividend-paying firms on short-term Mergers and Acquisitions (M&A) performance, others, such as Glambosky et al. (2020), report a positive effect. This discrepancy highlights the need for further investigation into the relationship between dividend-paying firms and Mergers and Acquisitions (M&A) performance, particularly in the context of Indonesia. This study aligns more with Glambosky et al. (2020), suggesting that dividend-paying firms positively impact short-term M&A performance.

Dividend Policy Consistency and Performance of Short-Term M&A

Consistency in dividend policy is crucial for maintaining investor confidence. Investors expect stability in dividend policies, which, if maintained, can lead to a more favorable market response to Mergers and Acquisitions (M&A) announcements (Glabosky et al., 2020). According to Glambosky et al. (2020), a consistent dividend policy positively influences short-term M&A performance, as reflected in unchanged dividend distributions before Mergers and

Acquisitions (M&A) announcements. Similarly, Ambarish et al. (1987) found that the market responds positively to Mergers and Acquisitions (M&A) announcements by companies that maintain or increase dividends.

The stability of a company's dividend policy is generally viewed more favorably by the market than a sudden increase in dividends, which might be perceived as an attempt to attract market attention before an Mergers and Acquisitions (M&A) announcement. Therefore, consistency in dividend policy is a key factor that can enhance the positive relationship between dividend-paying firms and short-term M&A performance.

Return on Assets (ROA) and Performance of Short-Term M&A

Return on Assets (ROA) is a crucial measure of a company's profitability and operational efficiency. ROA reflects how effectively a company uses its assets to generate profits, making it an important internal management ratio. A higher ROA indicates better operational efficiency, which can attract investors and positively influence the market's response to Mergers and Acquisitions (M&A) announcements. The greater the ROA, the better the market response to the Mergers and Acquisitions (M&A) announcement, strengthening the positive relationship between dividend-paying firms and short-term Mergers and Acquisitions (M&A) performance.

Grand Theory and Research Framework

The theories guiding this study include life cycle theory, signaling theory, agency theory, and bird-in-the-hand theory. These grand theories provide the conceptual foundation for understanding the relationships between the variables studied—namely, dividend-paying firms, dividend policy consistency, roa, and short-term Mergers and Acquisitions (M&A) performance.

Life Cycle Theory suggests that as companies mature, their focus shifts from investment opportunities to maintaining stable dividend payments, which is relevant when analyzing how dividend-paying firms perform in M&A activities. **Signaling Theory** posits that dividend payments serve as signals to the market about a company's financial health and future prospects, which can influence the market's response to M&A announcements. **Agency Theory** discusses the conflicts of interest between management and shareholders, particularly regarding the use of free cash flow, highlighting the importance of dividend policies as a mechanism for aligning interests. **Bird-in-the-Hand Theory** emphasizes shareholders' preference for certain dividends over uncertain future gains, underscoring the value of consistent dividend policies in maintaining investor confidence.

By integrating these grand theories, this study explores the hypothesis that dividend-paying firms positively impact short-term M&A performance, with this effect being moderated by dividend policy consistency and ROA, the hypothesis can be formulated as follows:

H1: *Dividend-paying firms have a positive effect on the performance of short-term Mergers and Acquisitions (M&A).*

H2: *The consistency of dividend policy strengthens the positive relationship between dividend-paying firms and performance of short-term Mergers and Acquisitions (M&A).*

H3: *Return on Assets (ROA) strengthens the positive relationship between dividend-paying firms and the performance of short-term Mergers and Acquisitions (M&A).*

Based on the explanation above, it can be concluded that dividend-paying firms have a positive influence on the performance of short-term Mergers and Acquisitions (M&A) and are strengthened by the consistency of dividend policy and Return on Assets (ROA). Thus, the relationship between the three variables can be described by the following research model:

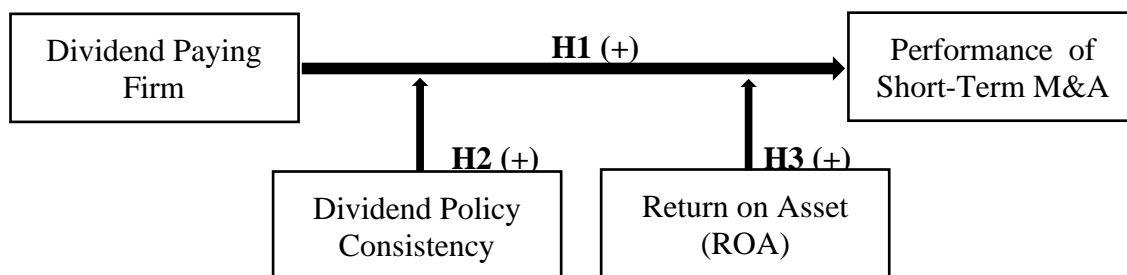


Figure 1. Research Model

Research Method

This study employs a quantitative research approach. Data is sourced from financial statements, company annual reports, the Thomson Reuters database, and Yahoo Finance. The research investigates the effect of the independent variable (dividend-paying firm) on the dependent variable (performance of short-term Mergers and Acquisitions (M&A)) and moderating variables (dividend policy consistency and ROA). Hypotheses are tested using statistical analysis tools, ensuring that the results are based on measurable data and are generalizable.

The data utilized in this study are secondary data obtained from companies that have conducted Mergers and Acquisitions (M&A) and are listed on the Indonesia Stock Exchange (IDX) during the period 2002-2021. The population consists of all public companies listed on the IDX that have engaged in M&A during this period.

A purposive sampling technique was employed to select the sample, focusing on companies that meet the following criteria: (1) bidder companies that have carried out mergers or acquisitions, (2) companies that have been listed on the IDX, and (3) companies with accessible and readable financial and annual reports. The sampling process involves identifying companies that meet these criteria and compiling the necessary data, resulting in a total sample of 150 observations.

The dependent variable in this research is performance of short-term M&A is measured using stock market indicators, specifically abnormal returns around the announcement of M&A. According to Zhou et al. (2019), abnormal returns provide insight into the market's response to M&A announcements by measuring stock price changes around the event. The performance of short-term Mergers and Acquisitions (M&A) is calculated by accumulating abnormal returns from two days before to two days after the announcement using the market-adjusted model method. The formula for Cumulative Abnormal Return (CAR) is as follows:

$$CAR_{i,t} = \sum [R_{i,t} - E(R_{i,t})] \dots \dots \dots (Eq.1)$$

Description:

CAR : Cumulative Abnormal Return on stock i on event t.

$R_{i,t}$: Actual return on stock i that occurs on day t.

$E[R_{i,t}]$: Expected return for stock i on day t.

The independent variable in this study is the dividend-paying firm, defined by the dividend policy one year prior to the M&A announcement. Data on dividend-paying firms are obtained from the company's annual report. A dummy variable is used to represent this, where companies that make dividend payments are coded as 1, and those that do not are coded as 0.

The moderating variables used in this study are consistency of dividend policy and Return on Assets (ROA). Consistency of dividend policy is a variable measures the stability of

a company's dividend payments over the three years preceding the M&A announcement. A dummy variable is used, with companies that consistently pay dividends for three consecutive years coded as 1, and others as 0. Return on Assets (ROA) indicates the operational efficiency of the company. It is calculated using the following formula:

$$ROA_{i,t} = \frac{Net\ Income}{Total\ Assets} \dots\dots\dots (Eq.2)$$

The control variable in this study is firm size, which represents the size of a company. Larger companies are generally considered to have better bargaining power in M&A activities. Firm size is measured using the natural logarithm of total assets:

$$Firm\ Size_{i,t} = \ln (Tota\ Assets) \dots\dots\dots (Eq.3)$$

Data analysis was conducted using Ordinary Least Squares (OLS) regression, which is well-suited for analyzing the relationships between variables in the dataset. The analysis process was performed using Stata, a statistical software that provides robust tools for regression analysis and is particularly effective for handling the type of panel data used in this study. The process began with descriptive statistics to provide an overview of the data, including measures of central tendency and dispersion. Model selection was then carried out to determine the most appropriate model structure. Classical assumption tests were conducted using Stata to ensure the validity of the OLS regression model, checking for multicollinearity, heteroscedasticity, autocorrelation, and normality. Hypothesis testing was performed through t-tests for individual coefficients and multiple regression analysis to explore the relationships between the variables, with Moderated Regression Analysis (MRA) employed to evaluate the impact of moderating variables. The coefficient of determination (R^2) was calculated to indicate the proportion of variance in the dependent variable explained by the independent and moderating variables. Additionally, the inclusion of the control variable (firm size) was tested to assess its impact on the relationship between the independent and dependent variables, all conducted using the analytical capabilities of Stata.

This study aims to determine the effect of dividend paying firms on the Performance of short-term M&A moderated by consistency of dividend policy and Return on Assets (ROA). This study uses the following model:

Model 1:

To determine the effect of dividend-paying firm and short-term merger and acquisition performance with firm size variable, it is necessary to build a regression equation model as follows:

$$M\&A\ performance_{i,t} = \alpha + \beta_1 DivPayingFirm_{it} + \beta_2 Firm\ Size_{it} + \varepsilon \dots\dots\dots (Eq.4)$$

Model 2:

To determine the effect of dividend-paying firms and the performance of short-term M&A moderated by the consistency of dividend policy and the control variable of firm size, it is necessary to build a regression equation model as follows:

$$M\&A\ performance_{i,t} = \alpha + \beta_1 DivPayingFirm_{it} + \beta_3 Consistency_{it} + \beta_4 DivPayingFirm * Consistency_{it} + \beta_2 Firm\ Size_{it} + \varepsilon \dots\dots\dots (Eq.5)$$

Model 3:

To determine the effect of dividend-paying firms and the performance of short-term M&A moderated by the Return on Asset (ROA) and the control variable of firm size, it is necessary to build a regression equation model as follows:

$$M\&Aperformance_{i,t} = \alpha + \beta_1 DivPayingFirm_{it} + \beta_2 ROA_{it} + \beta_3 DivPayingFirm * ROA_{it} + \beta_4 FirmSize_{it} + \varepsilon \dots\dots\dots (Eq.6)$$

Results and Discussion

The data analysis in this study was conducted using Ordinary Least Squares (OLS) regression with the assistance of Stata software, which is well-suited for handling panel data. The analysis proceeded through several stages, including descriptive statistics, model selection, classical assumption tests, and hypothesis testing. Descriptive analysis provided insights into the statistical properties of the research variables, including short-term Mergers and Acquisitions (M&A) performance, dividend-paying firms, dividend policy consistency, Return on Assets (ROA), and firm size.

Descriptive statistics offer a summary of the key characteristics of the data used in this study, as shown in Table 1. The descriptive statistics include the minimum value, maximum value, mean, and standard deviation for each variable. For short-term Mergers and Acquisitions (M&A) performance, measured by Cumulative Abnormal Return (CAR), the average value from 2002 to 2021 was 0.0724. The highest CAR observed was 0.4085, while the lowest was -0.4152. These values suggest that the market response to M&A announcements varied significantly, with some companies experiencing positive reactions leading to high CARs, while others faced negative responses.

Table 1. Statistic Descriptive

	N	Minimum	Maximum	Mean	Std. Deviation
M&A performance	150	-0,4152	0,4085	0,0724	0,0496
Dividen-paying	150	0	1	0,5200	0,5013
Consistency	150	0	1	0,2600	0,4401
ROA	150	-0,0860	3,475	0,1330	0,4081
Div-paying*Consistency	150	0	1	0,2533	0,4364
Div-paying*ROA	150	-0,0860	0,425	0,0464	0,0707
Size	150	0,3760	4,953	3,4800	0,8301
Valid N (listwise)	150				

The independent variable, dividend-paying firms, was measured using a dummy variable, with an average value of 0.52. This indicates that slightly more than half of the sampled companies paid dividends before making Mergers and Acquisitions (M&A) announcements. The consistency of dividend policy, a moderating variable, also used a dummy variable, with an average value of 0.26, suggesting that inconsistent dividend payments were more common among the sampled companies. The second moderating variable, ROA, had an average value of 0.1330, indicating that on average, the companies generated a 13.30% return on their assets. This metric is critical as it highlights the operational efficiency of the firms in utilizing their assets to generate profits, which can influence the market's response to M&A announcements.

The hypothesis testing involved three models, each designed to explore different aspects of the relationship between dividend-paying firms and short-term Mergers and Acquisitions (M&A) performance, with consistency of dividend policy and ROA as moderating variables.

Table 2. Performance of Short-Term M&A Regression Analysis Results

Variable	Performance of Short-term M&A		
Dividend-paying firm	1,639** (0,043)	1,288 (0,173)	1,736** (0,038)
Consistency		0,545 (0,695)	
Dividend-paying*Consistency		0,138 (0,828)	
ROA			0,219* (0,066)
Dividend-paying*ROA			1,771** (0,048)
Size	0,001** (0,038)	0,001* (0,054)	0,004* (0,068)
R-square	0,259	0,267	0,291
N	150	150	150

* significant at the level 10%

** significant at the level 5%

*** significant at the level 1%

Model 1 examined the direct effect of dividend-paying firms on short-term Mergers and Acquisitions (M&A) performance, with firm size included as a control variable. The results, shown in Table 2, indicate that dividend-paying firms have a significant positive effect on short-term M&A performance, with a regression coefficient of 1.639 and a significance level of less than 0.05. This finding is consistent with the bird-in-the-hand theory, signaling theory, and agency theory, which suggest that dividend payments send positive signals to the market, leading to better Mergers and Acquisitions (M&A) outcomes. The control variable, firm size, also had a significant positive impact on M&A performance, with a regression coefficient of 0.001. The R-squared value for this model was 0.259, indicating that 25.9% of the variance in short-term Mergers and Acquisitions (M&A) performance could be explained by the independent and control variables.

Model 2 introduced the consistency of dividend policy as a moderating variable. The interaction between dividend-paying firms and dividend policy consistency was positive but not significant, with a regression coefficient of 0.138 and a significance level greater than 0.05. This suggests that the consistency of dividend payments does not significantly strengthen the positive effect of dividend-paying firms on short-term Mergers and Acquisitions (M&A) performance. The R-squared value for Model 2 was slightly higher at 0.267, suggesting that the inclusion of the moderating variable explained an additional 0.8% of the variance in Mergers and Acquisitions (M&A) performance.

Model 3 incorporated ROA as a moderating variable. The interaction between dividend-paying firms and ROA had a significant positive effect on short-term Mergers and Acquisitions (M&A) performance, with a regression coefficient of 1.771 and a significance level of less than 0.05. This result indicates that higher ROA strengthens the positive relationship between dividend-paying firms and short-term M&A performance, implying that firms with better operational efficiency and profitability are more likely to experience positive market reactions to M&A announcements. The R-squared value for Model 3 was 0.291, indicating that 29.1%

of the variance in short-term M&A performance was explained by the variables included in the model.

The inclusion of the control variable, firm size, in all three models was crucial for isolating the effect of dividend-paying firms on short-term Mergers and Acquisitions (M&A) performance. The consistent significance of firm size across all models suggests that larger companies generally experience better Mergers and Acquisitions (M&A) outcomes, likely due to their greater resources and market influence. This finding supports the notion that firm size plays a critical role in Mergers and Acquisitions (M&A) success, and controlling for this variable ensures that the observed effects of dividend-paying firms and moderating variables are not confounded by differences in firm size.

The results of this study support the hypothesis that dividend-paying firms generally achieve better short-term Mergers and Acquisitions (M&A) performance compared to non-dividend-paying firms. However, the impact of dividend policy consistency as a moderating variable was not significant, suggesting that consistency alone does not enhance Mergers and Acquisitions (M&A) performance. In contrast, ROA was found to be a significant moderator, indicating that operational efficiency and profitability are key factors that can strengthen the positive relationship between dividend payments and Mergers and Acquisitions (M&A) success. These findings align with existing theories and contribute to the understanding of how dividend policies and firm performance interact to influence Mergers and Acquisitions (M&A) outcomes.

Conclusion

Based on the results of research using data from non-financial companies that conducted Mergers and Acquisitions (M&A) and were listed on the Indonesia Stock Exchange (IDX) during the period 2002 to 2021, it is concluded that dividend-paying firms have a positive effect on a company's short-term M&A performance. Companies that pay dividends are more favorably received by the market when announcing Mergers and Acquisitions (M&A) compared to companies that did not pay dividends in the preceding year. This finding aligns with theories that suggest dividends serve as a positive signal to the market, enhancing investor confidence and leading to better short-term performance outcomes.

The study's findings have several implications for corporate managers and investors. For managers, the positive impact of dividend payments on short-term Mergers and Acquisitions (M&A) performance suggests that maintaining a dividend-paying status could be a strategic tool for ensuring favorable market reactions during Mergers and Acquisitions (M&A) activities. For investors, the results indicate that companies with a history of dividend payments and strong operational performance, as reflected in ROA, are likely to generate better returns in the short term following Mergers and Acquisitions (M&A) announcements.

Despite its contributions, this study has certain limitations. The analysis is limited to non-financial companies listed on the IDX, which may not fully capture the diverse range of industries and markets that could influence the relationship between dividend policy and Mergers and Acquisitions (M&A) performance. Additionally, the study focuses on a single country, which limits the generalizability of the findings to other contexts.

Future research could address these limitations by expanding the scope of the study to include cross-country samples, thereby enhancing the generalizability of the findings. Additionally, increasing the sample size and including a more diverse set of industries could provide a more comprehensive understanding of how dividend policies impact Mergers and Acquisitions (M&A) performance across different market conditions. Moreover, further investigation into the role of dividend policy consistency could explore whether different time frames or alternative measures of consistency yield different results.

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