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# Dividend Policy and Firm Performance: The Case of Shariah-Compliant Non-Financial Firms in Pakistan

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## Abstract

This study examines how dividend policy affects the performance of Shariah-compliant (SC) non-financial firms in Pakistan. These firms operate under Islamic law, which restricts interest-based and speculative activities. Because of these rules, their financial structures differ from conventional firms. The study uses data from 2013 to 2023 for all non-financial SC firms listed on the Pakistan Stock Exchange. The screening criteria of Karachi Meezan Index (KMI) were used to identify these firms. A fixed-effects model was applied after conducting the Breusch–Pagan Lagrange Multiplier (BPLM) and Hausman tests. The results show that the dividend payout ratio (DPR) has a significant adverse effect on firm performance. Firm size (FS) and sales growth (SG) have positive, significant effects, while leverage has an adverse, significant effect. Dividend yield (DY) and dividend per share (DPS) were not significant. The findings support the agency, bird-in-hand, and signaling theories. The study contributes to the limited research on Islamic equity markets in Pakistan and shows how dividend policy influences profitability in Shariah-compliant firms. The results can help investors, managers, and policymakers design better dividend policies and strengthen Islamic financial governance in Pakistan.

**Keywords:** Dividend policy, Firm performance, Shariah-compliant, Dividend payout ratio, Dividend yield, Dividend per share

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# 1. Introduction

## 1.1 Background

A company's dividend policy (DP) is a strategy that determines the portion of profits allocated to shareholders, with the remaining amount reserved for future investments. If management decides to distribute dividends, the internal funding source will be reduced due to lower profits. On the other hand, if management decides to retain dividends, it will improve funding from internal resources. (Rahma, 2024). A DP determines the proportion of profits to be distributed to shareholders, aiming to support and ensure shareholders' well-being (Putri, 2023). Previous studies confirm the positive effect of DP on firm performance (Bakri et al., 2024). The authors highlight that paying dividends cannot increase shareholder value and that dividends have no positive effect on firm value. Dividend payment can mitigate agency problems and signal future profitability (Burhop & Selgert, 2025).

Most of the previous studies are based on non-SC firms. Shariah refers to Islamic law, derived from the teachings of the Prophet Muhammad (SAW), as found in the Hadith and the Quran. Companies that do not comply with Shariah engage in activities that make them unsuitable for Muslim investors. Three factors are identified as haram: *Gharar* (uncertainty), *Maisir* (gambling), and *Riba* (interest). SC companies must undergo audits, leading non-SC (conventional) companies to have a higher debt-to-asset ratio than their SC counterparts. A firm must meet Shariah screening criteria to distinguish between SC firms and NC firms. (1) Based on the principles issued by SECP and Shariah Advisory Boards, SC firms may not be involved in activities such as alcohol, pork, gambling, pornography, conventional activities (interests), tobacco, and weapons manufacturing. The SC dividend was introduced to meet the needs of Muslim investors seeking returns in the stock market. As the number of Muslim communities continues to grow worldwide, there is an increasing demand for SC investment options like dividends (Bakri & Yong, 2023).

Many studies have been conducted in Pakistan and around the world on the impact of DP on firm performance, but they have primarily focused on conventional firms. The influence of DP on Shariah-compliant firms has received little attention, especially in Pakistan. One previous study examined the impact of DP on shareholders' wealth in SC firms. In this study, the focus is on SC non-financial firms. SC firms (such as energy, manufacturing, and services) are required to operate in accordance with Islamic financial principles and to refrain from engaging in speculative activities, including by excluding banks and financial institutions. Due to these unique characteristics, SC firms are an appropriate context for examining how dividend policy affects the performance of a firm (Akbar et al., 2025). The

impact of DP on these firms is relatively less explored in Pakistan compared to globally. Nonetheless, research in Pakistan remains limited. To attract Muslim investors to the stock market, business owners must adhere to fundamental business practices outlined by Shariah. This study is confined to Pakistan due to its status as a large Islamic financial market. Pakistan is a predominantly Muslim country, and Shariah principles underpin most investors' decisions. According to the Global Islamic Economy Report 2021, Pakistan ranks as the seventh most developed Islamic financial market. Additionally, the 2021 re-weighting of the KSE Meezan 30 index indicates that nearly 60% of companies are SC[1]. Furthermore, the PSX received the 2021 Best Islamic Stock Exchange Award at the Global Islamic Finance Awards (GIFA) (Nam & Heshmati, 2025).

These characteristics make the Islamic market a critical focus for this study.
However, the issue of dividends for SC companies in Pakistan has not received much attention in the literature. Religion in Pakistan enhances managers' intrinsic motivation and positively influences their ethical behavior. Therefore, beyond individual firms, aligning commercial entities with Shariah (Islamic values) helps reduce agency conflicts. Shariah is the basis of responsibility and the primary source of authority in Islam, derived from principles that all believers are expected to adhere to. According to Islamic teachings, individuals are Allah's only agents or custodians. They are allowed to use and manage these resources under Shariah laws. Previous studies explore the effect of DP on firm performance; this study focuses on SC non-financial firms.

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*(1) By the KMI and SECP (2021) criteria:*
*(a) The debt-to-total-assets ratio must be less than 37% (or 33% in some cases). (b) Less than 5% of total revenue must originate from non-compliant income (haram). (c) The ratio of net liquid assets to market capitalization needs to be below 49%. (d) The amount of assets or securities that bear interest should be kept to a minimum.*

In light of the above discussions, the current study aims to address the literature gap by examining the effect of DP on the firm performance of non-financial SC firms in Pakistan. The study builds on established theories by adding DP indicators, including the DPR, DY, and DPS, and by evaluating firm performance using recognized metrics such as Return on Assets (ROA). Moreover, the research considers additional firm-specific factors —FS, GR, and Lev —to provide a detailed and comprehensive analysis. The sample includes all non-financial dividend-paying SC listed firms in Pakistan from 2013 to 2023. Data for these firms were obtained from the Companies' annual reports and the PSX for the period of 2013–2023. Firms not listed during the study period or with negative equity are excluded from the sample. Panel data methodology was employed based on the findings of diagnostic tests, such as BPLM and the Hausman test. This investigation recognizes that the operational and financial

environments of these organizations differ from those of conventional companies, reflecting their commitment to Islamic principles. This study fills a gap in current literature and enhances understanding of how DP can affect performance within an Islamic finance context. The study provides specific implications. That is, Policymakers design policies for both conventional and Islamic companies; however, this research focuses on policies that specifically influence SC firms.

This study is beneficial because one of the previous studies examined that DPR, DPS, and EPS are strongly impacting the shareholder wealth of SC firms, and also compares SC with non-SC firms. (Akbar et al., 2023). The growing importance of the Islamic finance sector and the ethical considerations of Muslim investors have led to greater emphasis on Shariah compliance in today's business practices across the global economy. Muslims obey Shariah, the Islamic legal framework derived from the Quran and Sunnah, to guide every facet of their lives, including their business dealings and procedures (Asif & Akhlaq, 2023). The author highlights that profitability, prior dividends, and liquidity have a significant impact on dividend behavior, given investors' motivations (Farooq et al., 2024). PSX's dividend payout hit a record of 500 billion in 2021. One of the main insights of this study is to inform the community about Islamic acceptable financing. Despite this, businesses that follow Shariah have limited options for conducting their operations. Companies that comply with Shariah and demonstrate strong governance often deliver exceptional performance. SC firms offer investors alternatives (such as creating a portfolio with minimal unsystematic risk) to identify investment opportunities that are free of ethical issues, supported by tangible assets, and free of speculative activities.

## 2. Literature Review

### 2.1 Dividend Policy and Firm Performance of Non-SC Firms

The non-SC company engages in practices that make it illegal for Muslims to invest. Three things deemed haram —Gharar (insecurity), Maisir (gambling), and Riba (usury) — are present in the non-SC company. Because SC firms must undergo an audit, non-SC (conventional) firms have a larger debt-to-asset ratio than SC firms. (Ashari Bakri & Chia Yong, 2023). According to Fatwa DSN-MUI No. 80/DSN-MUI/III/2011, equities that have undergone screening in the capital market in accordance with Islamic principles are known as Islamic stocks. The criteria used to screen SCFs are based on business practices that are forbidden because they go against Islamic law, such as 1) gambling, 2) trade of haram products, 3) interest-based banking or financing, 4) trade that involves gambling (Maisie) and speculation (gharar), 5) manufacturing, distribution, trade, and offering goods or services

which are forbidden due to their features (haram li-dating), non-contents (haram Alighieri), or unfair ethics; 6) conducting bribery-related activities (rishwah). Additionally, screening-related financial ratios, such as interest or prohibited unpacifically, the interest-based liabilities to total assets ratio must be less than 45%. Every May and November, screenings are carried out to ensure the companies follow Shariah law (Nikmah & Hung, 2024). The practice of Riba and other interest-based money-to-money trade is forbidden under Shariah. Islam limits the Riba amount of any commercial activity and guides how to handle the profits of non-Shariah companies (Doruk et al., 2025).

Non-SC businesses claim that dividend policies impact business performance. Many empirical studies that the authors evaluated indicate that profitability, LEV, and liquidity affect dividend policies, according to several earlier studies cited in this literature review. A company's size, profitability, LEV, and liquidity affect its value. Dividend policies also impact the company's value. Additionally, it has been realized that DP can reduce the effects of liquidity and profitability on firm value. Still, they cannot reduce the impact of debt (Haryono et al., 2024). The author explores how FS, GR prospects, profitability, and risk significantly influenced the dividends of non-SC firms. All examined factors in the panel quantile approach were significant drivers of dividends for both Shariah and non-SC firms, except those at the 0.50 quantile for non-compliant businesses (Bakri & Yong, 2023).

### 2.2 Dividend Policy and Firm Performance of SC Firms

The Islamic legal code, known as Shariah, is based on the Qur'an and the Sunna and governs individual and collective behaviour (Nikmah & Hung, 2024). According to earlier research, high dividend payments indicate low agency difficulties, sound corporate governance practices, and the management's good faith. The fact that SC businesses must have modest levels of LEV, accounts receivable, cash holdings, and interest-bearing securities is just one of the numerous reasons why their dividend determinants differ from those of non-SC businesses (Bakri & Yong, 2023).

When employing a linear regression technique, the dividend policies of the SC and non-SC companies differ. Similarly, when using a quantile regression strategy, the dividend policies of the SC and non-SC companies differ (Bakri & Yong, 2023). Ben-Nasr and Ghouma suggest that Shariah compliance may have either a positive (investment-constraint hypothesis) or a negative (finance-constraint hypothesis) impact on dividend payments. Due to their limited investment prospects, SC firms often distribute their available cash flows as dividends. On the other hand, these free cash flows could be retained by the SCFs due to

limited options for raising money for new projects. According to the author, the capital structure of Islamic businesses featured minimal debt. They observed that these businesses struggle to reduce their debt levels to an ideal level. Retained earnings are the source of money in this scenario. As a result, stockholders receive fewer dividend payouts. Studies demonstrating the beneficial effects of SCs on dividend distributions predominate in the literature (Zaigham et al., 2024).

According to a Baker and Weigand poll, investors' perception of the value of cash dividends is declining over time. Their study indicates that companies adopt a controlled dividend strategy instead of a residual DP (Ishfaq et al., 2024). Nevertheless, from the investor's standpoint, this DP is the one they favor the most. Since the company cannot turn a profit without engaging in initiatives with positive cash flow, investors view this policy as reasonable. Therefore, reinvesting money is more important than distributing dividends to shareholders. Risk-tolerant investors prefer a residual DP. When dividends are paid, they take advantage of them and look for capital gains. As a result, investors' investment decisions are unaffected even if the company does not pay dividends. Thus, the current study aims to ascertain how working capital and capital expenditures affect the company's DP (Wirama et al., 2024). The value of shareholders is the sole factor significantly affected by the DP; it is not significantly affected by firm value. The findings indicate that neither dividend payments nor DP appears to impact company value when using simultaneity equations substantially (Rahma, et al 2023.).

## 2.3 Hypothesis Development

### 2.3.1 Dividend Payout Ratio and Firm Performance

Several researchers disputed the link between dividend payments and business value or corporate performance. However, the author found a strong, positive correlation between dividend payments and business performance (Diab et al., 2024). Return on assets positively impacted by the DPR (Prihandoko & Abadiyah, 2024). A company's DP may impact its share price through payouts and distributions. A high ratio may indicate that a business has enough cash to pay dividends on its stock. The dividend payout ratio shows how much of the company's net profits are distributed as dividends, providing a clear explanation of how the company's DP is structured (Muktiadji et al., 2024).

$H_1$: Dividend payout has a positive effect on Firm performance.

### 2.3.2 Dividend Yield and Firm Performance

ROA, FS, and DY are all positively correlated (Amir et al., 2024). The DY positively impacts stock performance. (Muktiadji et al., 2024.). In contrast, there is a high positive correlation between DY and projected return for the New York Stock Exchange (NYSE), and variations in DY have a negative and substantial impact on the explanation of stock returns in the trading and service sectors (Sim Foong et al., 2007).

$H_2$: DY has a positive impact on Firm Performance.

### 2.3.3 Dividend per Share and Firm Performance

The study's findings suggest that DPS has no impact on the company's success because the significance threshold for DPS is 0.5465. The regression coefficient is 0.000270 (Perusahaan et al., 2023). The DPS significantly impacts the market price per share (MPPS) (Khadka & Gaire, 2024). There is a nonlinear association between DPS and financial return. (Heshamt et al., 2025).

$H_3$: DPS negatively impacts firm performance.

### 2.3.4 Firm Size and Firm Performance

A firm's size can be measured by analyzing its total earnings  how much cash it generates or by its asset base. Larger companies are more likely to use both internal and external capital sources. Strong business development and growth show up in a large company size, which can raise the value of the firm (Ryke et al., 2024). FS is a variable that can impact firm performance positively and has a significant impact on company performance (Rios, 2014). FS has an impact on Company Performance (Ryke et al., 2024).

$H_4$: FS has a positive and significant influence on firm performance.

### 2.3.5 Sales Growth and Firm Performance

Sales GR is calculated as current sales minus previous sales divided by previous sales (Jamadar et al., 2024). According to the sales GR, the firm is creating investments at a higher rate than expected, so that it will overinvest Sihombing et al., (2024). GR has a positive effect on firm performance (Ngoc Bach et al., (2024). The sales GR has a positive and significant impact on firm performance (Veeravel et al., 2024).

H5: Sales growth has a positive effect on firm performance.

### 2.3.6 Leverage and Firm Performance

The ability of a company to effectively manage its finances by taking on debt to enhance the wealth of its owners and investors is known as LEV (Ishak, 2024). LEV is a technique used by the firm to assess funding decisions. This can be used to estimate how effectively a company can utilize its equity to repay its debt. Investors analyze a business's ability to manage debt to cover firm activities effectively, and LEV can affect a firm's value (Sihombing et al., 2024). LEV has a negative and significant impact on firm performance (Veeravel et al., 2024). According to studies by Sihombing et al. (2024), Sasongko (2019), and Timotius & Setyawan (2023), LEV strengthens the value of a company. this positive trend suggests that the higher the LEV, the larger the firm value. Whereas studies by Kolamban et al. (2020), Rachmi & Heykal (2020), and Yuwono & Aurelia (2021) highlight that leverage does not affect business value (Sihombing et al., 2024).

$H_6$: LEV has a negative effect on firm performance.

## 2.4 Relevant Theories

Agency theory tackles the disputes between shareholders and management (Elhabib, 2024). According to the theory, agents may prioritize their self-interest over the best interests of the principals, which could lead to conflicts of interest between the two parties. A firm's management team decides how much of its profits should be paid out as dividends to shareholders, known as the DP (Jamadar et al., 2024). So, agency theory relates to this study; if the conflicts between principals and agents are minimized, a large number of investors will be attracted to invest their capital. Regular dividend payments can act as a monitoring mechanism. Economist Myron J. Gordon first proposed this concept in the 1960s. According to the theory, investors would rather have the guarantee of present earnings than the uncertainty of future returns. It claims that a company's existing dividends determine its worth rather than its potential for future growth. Empirical studies strengthen the theoretical framework. As per Lang and Litzenberger (1989), the stock prices of companies with fewer opportunities to invest respond more favorably to dividends than those of companies with plenty of growth prospects. According to research, when there are no profitable investment opportunities, this demonstrates that shareholders prefer dividends to guarantee efficient use of resources. Companies with high agency conflicts often continue to pay out higher dividends to comfort investors and avoid managerial misconduct (Ebrahim Bazrafshan, 2025). This theory believes that rules, instruments, or processes are the only ways to control the agency problem, which is an unavoidable fact. The dividend is one of the most widely utilized or suggested tools by scholars to mitigate agency problems. Jensen's 1986 free cash

flow hypothesis, which holds that dividends are paid to shareholders to keep managers from investing in unsuccessful projects and, in the worst situation, for their own personal interest. We have so determined that dividends should lessen the agency problem based on this idea (Bakri, Ayub, et al., 2024). According to the "bird in hand" theory, shareholders choose dividend payments over capital gains (retained earnings) (Alasfour et al., 2023). Therefore, the portion of income that is reinvested for further growth provides the market with a positive indication and raises the share price for the future. Therefore, the shareholder wants to receive the dividends and reinvest them by today, rather than retaining the earnings for reinvestment purposes (Akbar et al., 2023). A study by Baker, Farrelly, and Edelman (1985) shows a positive correlation between a company's stock price and dividend yield, which empirically supports the Bird-in-Hand Theory. According to the results, firms that give greater dividend yields are linked to higher stock prices, supporting the theory's argument that dividend payments have a favorable effect on investor views and, as a result, stock valuation (Kumar et al., 2024). The signaling theory states that a company's DP can provide insight into its growth, profitability, and management's level of confidence in the company's overall performance (Jamadar et al., 2024). This theory also states that strong profitability reflects the company's assets performing well, and the market has also reacted positively (Rahma et al., 2023). The asymmetric information concept, which posits that a company's management possesses more information than its investors or shareholders, forms the foundation of the signaling theory. Consequently, it uses dividends to communicate confidential information to investors. Investors see it positively if management pays more than expected dividends, and vice versa. It suggests the market receives a signal from a company's DP. As a result, management needs to understand this and adjust their DP appropriately (Akbar et al., 2023). According to this theory, companies with a solid foundation and positive growth are more likely to pay dividends regularly, indicating confidence in their ability to generate sustainable profits. A sudden change in dividend policy, such as a reduction or omission, could be seen as a bad sign that the company is experiencing financial difficulties or is unsure of its future performance (Kumar et al., 2024).

## 3. Methodology

### 3.1 Data and Sample

This study used all non-financial SC-listed firms in Pakistan as a sample from 2013 to 2023 that paid dividends. The data were obtained from the company's annual reports and the PSX for the period 2013–2023 for the sample firms. Firms not listed during the study period and those with negative equity are excluded from the sample. The panel data methodology was employed based on the findings of diagnostic tests, such as the BPLM and the Hausman test.

### 3.2 Variables

The dependent variables in this study. Is firm performance measured through ROA? This paper builds on a previous study that examines the financial performance of ROA. This paper uses dependent variables, such as ROA, to determine how independent variables affect them and to provide investors with useful information. This research uses independent variables related to DP, such as DPR, DY, and DPS, to assess the firm's financial strength and analyze their impact on firm performance. The control variables of the current study are the FS, GR, and LEV. The researcher chose control variables because they ensure accurate and trustworthy results, maintain consistency, prevent distortion, and facilitate a clear understanding of the relationships between the variables.

### 3.3 Model Specification

This study investigates the impact of DP on the performance of SC firms in Pakistan; for this purpose, we use the following model

$$ROA_{it} = \propto + \beta_1 DPR_{it} + \beta_2 DY_{it} + \beta_3 DPS_{it} + \beta_4 FS_{it} + \beta_5 GR_{it} + \beta_6 LEV_{it} + \mu$$

Where β is the coefficient for the explanatory variable, α is the constant, and μ is the error term; ROA is the dependent variable for firm performance. DPR, DY, and DPS are independent variables, and FS, GR, and Lev are control variables.

**Table 3.1:** Variables Measurement

| Variables | Symbols | Measurement | References |
|---|---|---|---|
| Dependent Variables | | | |
| Firm performance Variable | | | |
| Return on Assets | ROA | Net income divided by total assets | (Alasfour et al., 2023) |
| Independent Variables | | | |
| Dividend Policy Variables | | | |
| Dividend Payout Ratio | DPR | Dividend per share divided by earnings per share | (Zaigham et al., 2024) |
| Dividend Yield | DY | Dividend per share divided by price per share | (Akbar et al., 2023 |
| Dividend Per Share | DPS | Dividend paid divided by the number of common shares outstanding | (Akbar et al., 2023) |
| Control Variables | | | |

| | | | |
|---|---|---|---|
| Firm's Size | FS | N Log of the total assets | (Guizani et al., 2023) |
| Growth | GR | Current sales minus previous sales divided by previous sales | (Jamadar et al., 2024) |
| Leverage | LEV | Total debt divided by total assets | (Zaigham & Tariq, 2024) |

*Note: The table shows all variables and their measurement with references*

*Source: Author's own work*

ROA is the dependent variable in this study. The researcher measures ROA as net income divided by total assets (Alasfour et al., (2023). The study's independent variables are DPR, DY, and DPS, which measure DPR as dividend per share divided by earnings per share. (Zaigham et al., 2024), DY as dividend per share divided by price per share (Akbar et al., 2023, and DS as dividend paid divided by the number of common shares outstanding (Akbar et al., 2023). The study control variables are FS, GR, and LEV. The author measures FS as the Natural Log of total assets (Guizani et al., 2023), GR as current sales - previous sales / previous sales (Jamadar et al., 2024), LEV is measured as total debt / total assets (Zaigham & Tariq, 2024.

## 4. Results and Discussions

### 4.1 Descriptive Statistics

Table 2 shows a review of the descriptive data for the variables used in the study, which examines how dividend policies affect the performance of Pakistani non-financial SC firms. The average ROA of 6.89% and a standard deviation of 7.21% suggest a moderate level of operational efficiency of the firm. The sample's profitability varies significantly, ranging from 0.19% to 34.92%. The high standard deviation of 91.67% and the average DPR of approximately 5.13% indicate that many firms distribute profits unevenly among shareholders. DY has an average of 3.06% and a SD of 4.29% with a min of 0 and a max of 21.96. % shows substantial variation in DYs across firms.

**Table 3.2**: Descriptive Statistics

| Variable | Obs | Mean | Median | SD | Min | Max |
|---|---|---|---|---|---|---|
| ROA | 1551 | .06898 | .0438 | .07205 | .002 | .3492 |
| DPR | 1551 | .31542 | .0785 | .91670 | -2.856 | 6.0538 |
| DY | 1551 | 3.0601 | 1.49 | 4.2922 | 0.00 | 21.96 |
| DPS | 1551 | 7.6376 | 1.000 | 23.946 | 0.00 | 180 |
| FS | 1551 | 6.0348 | 6.7479 | 2.3044 | .014 | 8.8472 |
| GR | 1551 | .13063 | .0649 | .37287 | -.751 | 2.0164 |
| LEV | 1551 | .14734 | .103 | .15548 | 0.00 | .6512 |

***Notes:*** *This table shows the descriptive statistics, including mean, median, SD, and number of observations*
*Source: Author's own work*

The average DPS is 7.03, with a high SD of 23.95 and a maximum of 180, suggesting that most companies pay small dividends. The mean firm size is 6.05, with a standard deviation of 2.60. The range (0.0146 to 8.8472) indicates that the sample includes both small and large businesses. The firm growth rate is 13.06%, with a standard deviation of 57.3% (ranging from –75.09% to 201.64%), indicating that some firms experience lower growth while others experience extremely high growth. The average LEV ratio is 14.73% indicating SC restrictions on interest-bearing debt, with a SD of 15.58%. The minimum and maximum values range from 0 to 65.12%, meaning no firm will exceed the LEV ratio of 65%.

### 4.2 Correlation

The study's variables, with a focus on ROA as a measure of company performance, are shown in Table 3 along with their Pearson correlation coefficients. This analysis helps define their direction and strength. A weak positive correlation (r = 0.0642) is observed between the DPR and ROA. This means that a firm with higher profits pays out a large portion of dividends.

**Table 3.3*:*** Matrix of Correlations

| Variables | ROA | DPR | DY | DPS | FS | GR | LEV |
|---|---|---|---|---|---|---|---|
| ROA | 1.000 | | | | | | |
| DPR | 0.064 | 1.000 | | | | | |
| DY | 0.253 | 0.338 | 1.000 | | | | |
| DPS | 0.394 | 0.136 | 0.237 | 1.000 | | | |
| FS | 0.295 | 0.137 | 0.219 | 0.141 | 1.000 | | |
| GR | 0.167 | -0.005 | -0.005 | 0.005 | 0.122 | 1.000 | |
| LEV | -0.167 | -0.034 | 0.008 | -0.083 | 0.310 | 0.036 | 1.000 |

***Notes:*** *This table shows the correlation analysis for SC firms. ROA is the dependent variable, while DPR, DY, and DPS are the independent variables; the control variables are FS, GR, and LEV.*
*Source: Author's own work*

The results showed a moderate positive correlation between DY and ROA (r = 0.2533), suggesting that firms with stronger operational performance may yield higher returns. The DPS shows a positive relationship with ROA (r = 0.3944). This result suggests that a more profitable firm must pay more dividends per share in the context of SC firms, as signaling theory supports. FS also shows a moderate positive correlation with ROA (r = 0.2950), indicating that large businesses generate income from economies of scale and utilize their

resources more effectively. The GR and ROA exhibit a weakly positive correlation (r = 0.1675), indicating that growing businesses tend to achieve slightly higher returns, possibly due to sales-related benefits. ROA and LEV exhibit a negative correlation (r = -0.1673), suggesting that businesses with higher debt levels tend to be less profitable.

### 4.3 Variance Inflation Factor (VIF)

To assess multicollinearity among the study's variables, VIFs will be computed. Table 4 shows the VIF values for all variables included in the regression models.

**Table 4.1**: Variance Inflation Factor

| Variables | VIF | 1/VIF |
|---|---|---|
| DY | 1.212 | .825 |
| FS | 1.212 | .825 |
| DPR | 1.142 | .876 |
| LEV | 1.132 | .883 |
| DPS | 1.088 | .919 |
| GR | 1.016 | .984 |
| Mean VIF | 1.134 | |

**Source:** *Author's own work*

We found that all the VIF values are below 10. According to (Akbar et al., 2023), if these VIF values are less than 10. Therefore, we assume that this data set does not exhibit multicollinearity. The independent variables—DPR, DY, and DPS —along with the control variables—FS, GR, and LEV —do not show significant correlations with one another. Hence, the models do not exhibit multicollinearity.

### 4.4 BPLM and the Hausman Test

To validate the result, we choose a suitable estimator based on the data's nature. We employ two tests: first, the BPLM test to select between pooled OLS and random or fixed effects, and second, the Hausman test to choose between fixed and random effects. First, we employ the BPLM test. The test result was significant at the 5% level (p-value = 0.0000). Because the p-value is lower than 0.05, we reject the null hypothesis. This indicates significant panel-level variance, making the random-effects model more suitable than pooled OLS.

Secondly, we employ the Hausman test to choose the correct estimator between fixed and random effects. The result of the Hausman test was also significant (p-value = 0.0000), indicating that the fixed-effects model is preferred over the random-effects model. The random-effects estimator is inconsistent, and using the fixed-effects approach yields more reliable coefficient estimates in this situation.

**Table 4.2:** BPLM and the Hausman (1978) Specification test

| Test | SC firms |
|---|---|
| BPLM chibar2(01) | 1543.97 |
| *p*-value | 0.0000 |
| Hausman Chi-square | 39.045 |
| P-value | 0.0000 |

*Note: The table shows the result of the BPLM and Hausman test*
*Source: Author's own work*

To evaluate whether the fixed-effects model is more suitable than the random-effects model, a Hausman test was performed. The p-value is less than 0.05, suggesting that the variance in coefficients is both systematic and statistically significant. Consequently, in the best interest of the variability, the fixed-effects model is selected. The fixed-effects estimator is better suited for the data for estimating the correlation between DP and firm value.

### 4.5 Regression Analysis

The fixed-effects model was employed to examine the impact of DP and control variables on firm performance, as measured by ROA. The regression results are shown in Table 5. The DPR shows a statistically significant adverse effect on ROA. Probability value ($p < 0.01$), suggesting that higher payout ratios could be harmful to firm performance. In a previous paper, the author found a strong, positive correlation between dividend payments and business performance (Diab et al., 2024) and also, ROA is positively impacted by the DPR (Prihandoko & Abadiyah, 2024). This paper rejected H1 and found that DPR has a negative and significant effect on firm performance. DY and DPS are found to be statistically insignificant, indicating that they have no meaningful impact on ROA in this analysis. In the previous papers, the author found that DY has a positive impact on firm performance. (Amir et al., 2024;Muktiadji et al., (2024)The result of this paper rejects H2 and suggests an insignificant impact on firm performance.

**Table 4.3:** Regression Results

| ROA | Coef. | St. Err. | t-value | p-value | [95% Conf | Interval] | Sig |
|---|---|---|---|---|---|---|---|
| DPR | -.00846 | .00141 | -5.95 | 0.000 | -.011 | -.00568 | *** |
| DY | .00073 | 0.0004 | 1.60 | .0770 | 0.00 | .00154 | * |
| DPS | .00020 | 0.0001 | 1.08 | .1180 | 0.00 | 0.0004 | |
| FS | .01139 | .00087 | 12.50 | .0000 | .008 | .01311 | *** |
| GR | .02575 | .00314 | 7.80 | .0000 | .018 | .03191 | *** |
| LEV | -.12469 | .01113 | -10.98 | .0000 | -.145 | -.10285 | *** |
| Year | -.00152 | .00040 | -3.80 | .0000 | -.0023 | -.00074 | *** |
| Constant | 3.1005 | .80947 | 3.83 | .0000 | 1.513 | 4.688 | *** |
| R-squared | | 0.187 | Number of obs | | | | 1551 |
| F-test | | 46.193 | Prob > F | | | | 0.000 |
| Time Dummies | | Yes | | | | | |

*Source: Author's own work*

FS and GR show a positive and significant relationship with ROA. Probability value ($p < 0.01$), supporting the idea that larger and more rapidly growing firms generally achieve better performance. Previous literature shows that FS can impact firm performance positively and has a significant effect on Company Performance (Rios, 2014), (Ryke et al., 2024). Therefore, this paper agrees with H4 and H5. LEV is negatively and significantly correlated with ROA. A probability value ($p < 0.01$), suggesting that increased debt levels may harm profitability. In the previous literature, the authors found that LEV has a negative and significant impact on firm performance (Veeravel et al., 2024), (Sihombing et al., 2024). The result of this paper aligns with H6, confirming the same finding.

## 5. Conclusions

This study aims to assess the impact of DP on the performance of firms listed on the PSX from 2013 to 2023 using panel data regression analysis. We employed the fixed-effects model to draw conclusions based on the outcomes of the BPLM and the Hausman tests. A key method in panel data analysis is the fixed effect model. Unobserved heterogeneity, or factors that change between entities but remain constant over time, is taken into account; these variables may correlate with the regressors. The fixed effects approach eliminates the potential bias in OLS estimates, which is a problem, by isolating specific time-invariant features (Ebrahim Bazrafshan,. 2025). The results of the study indicate that DP has a significant influence on the performance of SC firms. The DPR, DY, and DPS serve as proxies for DP, with DPR demonstrating a statistically significant negative impact on firm

performance. In contrast, DY and DPS show no statistically significant effect on firm performance. Among the control variables, both FS and GR show a positive and significant relationship with ROA. LEV is found to have a negative and significant correlation with firm performance. Additionally, it was discovered that Agency, Bird-in-Hand, and Signaling theories are collectively relevant to SC firms. Agency theory suggests that excessive dividend payments can mitigate conflicts between managers and shareholders. (Guizani et al., 2023) says that dividend payments act as a control mechanism in emerging markets. Relevant to Pakistan, where corporate mechanisms are weak. The bird-in-hand theory suggests that paying higher, more regular dividends has a positive impact on investors, leading to higher firm value and better performance. Signaling theory signals to investors the stronger position of a firm, making it more attractive to potential investors and enhancing the firm's performance**.** (Ahmed et al., 2024) noted that dividend announcements influence stock price and market-based performance. This research presents specific implications. The findings of this study provide important information for the management of SC firms about the factors that influence a reliable DP and its impact on firm performance. This information will help them create an optimal DP that enhances firm performance. Additionally, it clearly illustrates how Shariah compliance affects the relationships among DP, FS, GR, and LEV. Shareholders and future investors can also benefit from this study's findings, as they gain a clearer understanding of the significant firm-specific factors and their influence on stock prices, enabling more informed investment decisions. Finally, it highlights the primary dividend theories relevant to Pakistan in the context of SC firms.

### 5.1 Limitations and Future Research

The current research focuses on companies from a single country —specifically Pakistan — limiting the broader applicability of the findings. As a result, further research on this topic should be conducted using a larger sample from various Muslim nations. Moreover, future investigations may include other firm-level and macroeconomic factors, such as corporate governance metrics, inflation rates, or interest rates, to gain a more comprehensive understanding of the dynamics influencing firm performance.

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