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IMPACT OF DIVIDEND POLICY ON FIRM PERFORMANCE: MODERATING ROLE OF CREDIT RISK

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ABSTRACT

This study examines the impact of Dividend Payout Ratio (DPR) on firm performance, measured by Return on Assets (ROA), in Indonesian banking companies, with Non-Performing Loans (NPL) as a moderating variable. Using secondary data from the financial statements of 11 banks listed on the Indonesia Stock Exchange (IDX) from 2019 to 2023, this research employs Moderating Regression Analysis (MRA) to test three hypotheses. The results indicate that DPR has a significant positive effect on ROA, supporting the hypothesis that higher dividend payouts enhance firm performance by attracting and retaining investors and signaling financial health. Conversely, NPL does not have a statistically significant direct effect on ROA, nor does it moderate the relationship between DPR and ROA. This suggests that while DPR is crucial for improving firm performance, the role of credit risk, as measured by NPL, does not significantly alter this relationship in the context of the studied banking companies. The R-squared value of the regression model is approximately 0.53, indicating that DPR and NPL explain 53% of the variability in ROA. These findings imply that dividend policies can be pursued independently of the current levels of non-performing loans, simplifying decision-making processes regarding dividend strategies. However, banks must continue to manage NPLs effectively for overall financial health. The study's limitations include a limited sample size and the exclusion of other potential moderating variables, suggesting areas for future research to provide a more comprehensive understanding of the factors influencing firm performance in the banking sector.

Keywords: Dividend Payout Ratio; Non-Performing Loan; Return on Assets.

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1. INTRODUCTION

In the field of banking performance review, numerous important financial indicators are absolutely important in determining the effectiveness and success of banks. One basic indicator of how well a financial organisation controls its assets to create profits is Return on Assets (ROA) (Haryono (2024). Comparatively to their total assets, ROA shows how lucrative a bank is and helps one evaluate its operational ability (Ozili, 2019). Furthermore influencing shareholder satisfaction and future capital funding policies (Fauzi & Rukmini, 2018) the Dividend Payout Ratio (DPR) offers insights into a bank's stance on profit distribution against retention. Among the several elements that affect DPR is Return on Equity (ROE), a surrogate for a bank's profitability (Budagaga, 2020).

Furthermore important indicators of loan portfolio quality and bank risk management effectiveness are the Non-Performing Loan (NPL) ratio (Sutrisno, 2023). High NPL levels point to more risk, therefore undermining stability and profitability. Research on the degree of NPLs has revealed how much a bank's financial health and performance may be influenced (Sutrisno, 2023).

In banking, liquidity management, credit risk, and capital sufficiency all affect efficiency and success as well (Jamal, 2023). Determining a bank's financial situation and capacity to remain profitable depend on these components. Key elements influencing a bank's whole risk profile and hence influencing its performance are liquidity risk, credit risk, and operational risk (Jamal, 2023).

In the banking industry, Dividend Payout Ratio (DPR), Non-Performing Loans (NPL), and Return on Assets (ROA) interact in a complicated manner under impact of several elements. Although current studies have investigated how NPL affects ROA and the link between Net Interest Margin (NIM) and ROA (Safitri, 2022), there is a knowledge vacuum on how NPL influences the relationship between DPR and ROA, particularly under varying economic conditions and banking policies.

Research showing a direct link between NPL and ROA have found that lower ROA levels are linked to greater NPLs and vice versa (Mustafa, 2024). Furthermore negatively affecting ROA (Mustafa, 2024; Ahmed et al., 2021) has been the quality of loan portfolios as seen by NPL ratios. Moreover, NPL has been found as a major determinant of bank profitability metrics including ROA and Return on Equity (ROE) (Mustafa, 2024; Ahmed et al., 2021).

Other factors, such interest rates, can also help to attenuate the effect of NPL on ROA; studies of traditional commercial banks (Safitri, 2022) reveal that interest rates can so influence the effect of NPL on ROA. While operational efficiency, bank size, and ROA have been linked to decrease NPLs, factors including credit growth, net interest margin, and loan loss provision have been found to raise NPLs (Ahmed et al., 2021).

Examining the moderating effect of Non-Performing Loans (NPLs) in the link between Dividend Payout Ratio (DPR) and Return on Assets (ROA) can help to improve the forecasting accuracy of financial models and hone risk management strategies inside banks. Banks can better match their dividend policies with the current risk environment by clarifying this link, hence optimising profitability and stability (Puspitaningtyas, 2019).

Studies have demonstrated how much NPLs could affect the stability and profitability of a bank. High NPL banks could find it difficult to get capital and other financing sources, which would increase funding costs and maybe lower the loan supply (Thornton & Tommaso, 2020). Rising NPLs also threaten financial stability and restrict banks' lending capacity by means of issues including rising credit card debt, societal pressures, and financial illiteracy (Napi, 2024).

Understanding bank profitability depends on a knowledge of the elements affecting NPLs and their effect on ROA. Furthermore influencing the relationship between NPLs and other financial statistics is the efficiency of banks (Jiang, 2024). Moreover, the size of a corporation can function as a moderating factor, therefore affecting the link between profitability and NPL. Emphasising the significance of considering company size while examining these correlations, this interaction increases the influence of profitability on NPLs (Nurhidayat et al., 2023).

This paper suggests to methodically look at how NPLs affect bank ROA by changing the effects of DPR. The main theory is that greater NPL ratios reduce the favourable effect of DPR on ROA, thereby suggesting that the advantages of strong dividend payouts in terms of asset returns are lessened when banks have larger loan defaults. Using econometric modelling, this study will examine data from numerous banks throughout several years to guarantee generalisability and resilience of the results. Emphasising the need of contextual financial strategies catered to loan portfolio quality, the results are projected to considerably contribute to academic research and offer pragmatic recommendations for bank management. By tackling these components, this study will close a significant knowledge gap and support the creation of more resilient banking procedures, therefore impacting perhaps global academic theories and actual banking operations.

Due to information asymmetry, signalling theory proposes that managers utilise dividend payouts to convey to external investors information on the future prospects or profitability of a company (Baker et al., 2019). The dividend payout ratio has been found to have a beneficial effect on firm value, so supporting both the bird-in-hand and signalling hypotheses (Rajan, 2024). Moreover, it has been shown that in microfinance firms the indirect

effect of the dividend payout ratio via return on assets is positive and noteworthy (Budhathoki, 2024). Based on signalling theory, dividends are seen as a good indicator for shareholders since big dividend distributions show strong after-tax gains (Wardani et al., 2022). Empirical results show that the capital ratio and bank size negatively influence dividend payout policies whereas earnings per share and cash flow positively influence them (Jabbar et al., 2023). Furthermore supporting dividends as important markers of a company's profitability and general state of affairs are signalling and information theories (Agrawal, 2021). With the effect of the dividend payout ratio on return on assets being a derived component of this connection, return on equity and return on assets significantly influence the link between the dividend payout ratio and a company's profitability (Aman, 2022).

A key component impacting the success of a company is its dividend policy. Baker et al. (2019) emphasised that dividend policy in Sri Lankan firms is influenced by factors like expected future earnings and cash on hand (Baker et al., 2019). In a literature review, Haryono (2024) found that there is a complicated relationship between dividend policy, financial performance, and firm value (Haryono, 2024).

In their study, Nguyen et al. (2021) confirmed that dividend policy plays a crucial role in determining how well firms perform in Vietnam. Njoku (2024) looked at how dividend policy affected Korean firms and found that it had a significant impact on their value. Margono and Gantino (2021) confirmed that firm size, leverage, profitability, and dividend policy all work together to determine firm value, with dividend policy having a particularly positive effect (Margono and Gantino, 2021).

In their study of non-financial listed companies in Sri Lanka, Jatoi et al. (2023) demonstrated that dividend policies have a significant impact on firm performance. Abeysinghe (2023) found a positive association between ROE, ROA, dividend policy, and sales growth. The results support the idea that dividend policy has a substantial impact on the value and performance of a company. In order to maximise their strategies for long-term growth and profit, businesses must have a firm grasp of this connection.

Important elements that greatly affect a company's performance are its credit risk and its dividend policy. In their analysis of non-financial enterprises' financial performance, Mushafiq et al. (2021) emphasise the substantial influence of credit risk. In order to optimise business performance, Li et al. (2019) stress the significance of knowing about credit risk. To improve financial performance and guarantee the long-term viability of enterprises, it is crucial to understand and manage credit risk, in addition to implementing suitable dividend policies.

An important indicator of a bank's asset quality and the efficacy of its risk management is the number of non-performing loans (NPLs). A decline in asset quality, as shown by high nonperforming loans (NPLs), causes loan loss provisions to rise and profitability to fall (Ozili, 2019). Additional research into the effects of nonperforming loans on the correlation between DPR and ROA is necessary. High nonperforming loans (NPLs) might put a damper on dividend payouts' potential to boost asset returns, according to the research. The reason behind this is because funds that could be used for effective investments or generous dividend payments are instead going towards paying off loans, which diminishes the positive impact of DPR on ROA (Napi, 2024). The correlation between nonperforming loans and dividend payout ratios is vital for dividend policy. The efficiency with which a bank may pay out dividends may be compromised if funds are diverted to cover nonperforming loans. For efficient risk management and profitability, it is crucial to comprehend the relationship between nonperforming loans (NPLs), dividend payouts, and a bank's financial performance. This study's three main hypotheses are derived from the literature review:

H1: DPR has a positive impact on ROA. This hypothesis posits that a higher Dividend Payout Ratio (DPR) leads to improved firm performance, as measured by Return on Assets (ROA). Previous studies have shown that companies with higher dividend payouts tend to attract and retain investors, thereby boosting market confidence and potentially enhancing financial performance indicators like ROA. The positive relationship between DPR and ROA suggests that a well-structured dividend policy can signal financial health and contribute to higher profitability.

H2: NPL has a negative impact on ROA. This hypothesis suggests that a higher Non-Performing Loan (NPL) ratio negatively impacts firm performance, as measured by ROA. High NPL ratios indicate deteriorating asset quality and increased credit risk, which can erode profitability by necessitating higher loan loss provisions and reducing the effective use of assets. The negative relationship between NPL and ROA underscores the importance of credit risk management in maintaining bank performance.

H3: NPL weakens DPR's impact on ROA. This hypothesis proposes that the presence of high NPL ratios weakens the positive effect of DPR on ROA. When banks face higher levels of non-performing loans, the benefits derived from high dividend payouts on asset returns are diminished. This moderating effect suggests that credit risk can significantly alter the relationship between dividend policies and firm performance, highlighting the need for banks to align their dividend strategies with their credit risk profiles.

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2. RESEARCH METHODS

This quantitative study uses the Non-Performing Loan (NPL) ratio as a moderator to examine the connection between the Dividend Payout Ratio (DPR) and Return on Assets (ROA) in Indonesian banking organisations. This study aims to use secondary data derived from financial reports of banks listed on the Indonesia Stock Exchange (IDX) between 2019 and 2023 to examine three primary hypotheses. Secondary data used in the study comes from bank businesses listed on the IDX and their financial statements and annual reports. These reports include all the necessary data for the study, including DPR, NPL, and ROA.

Table 1. Operational Definition of Variables

Variable	Instrument	Operational Definition	Measurement Scale	Formula
Dividend Policy	Dividend Payout Ratio (DPR)	Percentage of net income distributed as dividends.	Ratio	(Total Dividends Paid) / (Net Income) x 100%
Credit Risk	Non-Performing Loans (NPL)	Proportion of loans that are in default or close to default.	Ratio	(Non Perfoming Loans) / (Total Loans) x 100%
Firm Performance	Return on Assets (ROA)	Profitability relative to total assets.	Ratio	(Net Income) / (Total Assets) x 100%

Source: Processed Data (2025)

All 47 banking companies registered on the Indonesia Stock Exchange (IDX) between 2019 and 2023 make up the population for this research. The following factors were considered when selecting a random sample of eleven financial institutions: (1) financial institutions that will be listed on the IDX from 2019 to 2023, (2) financial institutions that will pay dividends from 2019 to 2023, and (3) financial institutions that will supply all the necessary financial data for the study. As a result of this decision, we have 55 data observations, collected over five years from 11 different organisations.

This study uses each banking company listed on the IDX as its unit of analysis. The study uses a longitudinal time frame, looking at data from 2019 all the way through 2023. To gain a better grasp of the interrelationships between the variables, this method permits the investigation of patterns and shifts across time. To examine the impact of DPR on ROA and the moderating role of NPL in this connection, the data is analysed using Moderating Regression Analysis (MRA). To learn how NPL affects the nature and direction of the connection between DPR and ROA, MRA is elected.

3. RESULTS AND DISCUSSION

This section presents the results of the data analysis and discusses the findings of the study. The objective of this research is to evaluate the impact of Dividend Policy, measured by the Dividend Payout Ratio (DPR), on Firm Performance, measured by Return on Assets (ROA), and to assess the moderating role of Credit Risk, measured by Non-Performing Loans (NPL), in Indonesian banking companies. The data analysis was conducted using Moderating Regression Analysis (MRA) to test the formulated hypotheses. The statistical analysis results, classical assumption test and the interpretation of the main findings are detailed in the following subsections.

3.1 Descriptive Statistics

The following table presents the descriptive statistics of the key variables used in this study. These statistics provide an overview of the central tendencies and variability within the data, offering insights into the distribution and characteristics of the variables across the sampled banking companies from 2019 to 2023. The descriptive statistics help to contextualize the subsequent analysis by highlighting the range, mean, and standard deviation of each variable.

Tabel 2. Descriptive Statistics

Descriptors	DPR (%)	NPL (%)	ROA (%)
Number of Samples	55.00	55.00	55.00
Average	48.74	2.41	2.30
Standard Deviation	17.27	0.95	0.96
Minimum	12.35	0.93	0.50
Maximum	85.27	4.48	4.22

Source: Processed Data (2025)

The average Dividend Payout Ratio (DPR) is 48.74% according to statistical data from 55 samples, with a large range across firms ranging from 12.35% to 85.27%. There is a wide range in the quality of loans made by different organisations, with an average of 2.41% for non-performing loans (NPL). Variations in the effectiveness of the company's asset utilisation are shown by the average Return on Assets (ROA) of 2.30%, which ranges from 0.50% to 4.22%. The data shows that the examined companies' dividend policy, asset quality, and operational efficiency vary. The sample companies' dividend distribution, loan quality, and asset utilisation efficiency are summarised in the table. Companies' varying approaches to risk management are borne out by the dissimilarities in DPR and ROA, which in turn reveal various strategies and operating conditions.

3.2 Classical Assumption Test

From what we can see from running the regression model through the classical assumption test, it passes the vast majority of the tests. The results of the multicollinearity test show that there is no substantial multicollinearity between the DPR and NPL variables, as they both have low VIF values of 1.01. There is no heteroscedasticity, according to the Breusch-Pagan test, which yields a Lagrange Multiplier statistic of 5.75 and a p-value of 0.04. In the absence of statistically significant autocorrelation, the Durbin-Watson autocorrelation test yields a result of 1.40. Lastly, the residuals are normally distributed, as shown by the 3.16 statistic and p-value of 0.21 produced by the Jarque-Bera residual normality test. Despite a few minor signs of heteroscedasticity, this regression model generally satisfies the classical requirements.

3.3 Moderating Regression Analysis (MRA)

The following table presents the results of the Moderating Regression Analysis (MRA), which was conducted to examine the impact of DPR on ROA, and to assess the moderating effect of NPL on this relationship. The analysis aims to determine whether NPL significantly alters the influence of DPR on ROA in Indonesian banking companies. The table includes the coefficients, standard errors, t-values, and significance levels for the regression model, providing a comprehensive view of the relationships among the studied variables.

Tabel 3. Results of Moderation Regression Analysis Test

Variable	Coefficient	Std. Error	t-value	Sig.
Intercept	1.42	0.69	2.06	0.04
DPR	0.04	0.01	2.68	0.01
NPL	-0.30	0.26	-1.16	0.25
DPR_NPL_Interaction	-0.00	0.01	-0.36	0.72

Source: Processed Data (2025)

The results of the Moderation Regression Analysis show that the dividend payout ratio (DPR) has a positive effect on return on assets (ROA), lending credence to the idea that larger dividend distributions boost company performance. Even though the NPL ratio is negative (-0.30), it is not statistically significant (sig.=0.25), hence NPL does not seem to have a major detrimental impact on ROA here. In addition, NPL does not attenuate the link between DPR and ROA, as indicated by the interaction term between the two variables, which has a coefficient of -0.00 and a sig. of 0.72. Thus, although dividend policy has an important role in enhancing business performance, this analysis does not show that credit risk, as assessed by NPL, acts as a moderator.

3.4 Coefficient of Determination Test

Based on the regression analysis, the R-squared value is close to 0.53. So, the dividend payout ratio (DPR) and non-performing loans (NPL) account for 53% of the variation in return on assets (ROA). Although DPR and NPL are critical factors in predicting ROA, other factors account for 47% of the variability in ROA, indicating that the model has a modest level of explanatory power. Market circumstances, operational efficiency, and larger economic variables are some of the additional considerations that could be considered. Therefore, although the model does a good job of explaining the connection between DPR, NPL, and ROA, a fuller investigation that takes other factors into account might shed light on the banking industry's performance drivers.

3.5 The Impact of DPR on ROA

The Moderation Regression Analysis test found that DPR positively and significantly affects ROA and that this relationship is statistically significant. In particular, DPR has a coefficient of 0.04 and a t-value of 2.68 and a

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significance level of 0.01. A positive coefficient like this one means that, everything else being equal, the ROA goes up by 0.04 units for every unit increase in the DPR. This conclusion is highly unlikely to have occurred as a consequence of random chance, as shown by the statistical significance of the association (sig. of 0.01). It follows that DPR and ROA are positively related. This confirms what previous research has shown: that a higher DPR can improve a company's performance in three ways: by luring and keeping investors, by increasing market confidence, and by indicating financial stability and health.

One strategic option that banking organisations can use to improve their overall performance is keeping a robust dividend payout policy. According to research, banks that pay out a larger part of their profits as dividends are more likely to be profitable and use their assets efficiently (Budagaga, 2020). This is because dividend payments show that a firm is doing well financially, which boosts investor confidence and brings in more money, which helps the company grow (Budagaga, 2020).

Furthermore, dividend policy is an essential part of banking sector financial management (Rawal, 2024). Investors can feel more secure about a company's future profits if it pays out dividends (Ibrahim et al., 2023). Stable dividends are seen favourably by shareholders because they indicate the firm's stability and sustainability (Heriansyah, 2023). Also, larger banks that pay dividends tend to have more consistent payout policies and less earnings volatility, so they don't have to manipulate their results as much to keep paying dividends (Tran & Ashraf, 2018).

Also highlighted is the connection between dividend policy and company performance; specifically, how dividend payouts affect profitability (Aman, 2022). The stock prices of commercial banks are affected by a number of factors, including dividend policies, which have a significant impact on stock prices (Gurung, 2023).

3.6 The Impact of NPL on ROA

The Moderation Regression Analysis found that there is no statistically significant relationship between the Non-Performing Loans (NPL) ratio and Return on Assets (ROA). In particular, NPL has a -0.30 coefficient, a t-value of -1.16, and a sig. of 0.25. While the sig. shows that the link is not statistically significant at conventional levels, the negative coefficient implies that there may be an inverse association where higher NPLs are associated with lower ROA.

Since the results are not statistically significant, we cannot say with certainty that changes in the NPL ratio significantly affect ROA within this study. Put simply, the profitability and efficiency of asset utilisation in the sampled banking institutions over the study period were not consistently and reliably affected by variations in credit risk, as assessed by the fraction of non-performing loans (Thornton & Tommaso, 2020).

This observation could be explained by a number of things. Management quality, market circumstances, and other risk management strategies are not part of the model but may have a more significant impact on ROA. Furthermore, banks might have effective measures to reduce the impact of nonperforming loans (NPLs), such as robust loan recovery procedures or sufficient provisions for loan losses (Mustafa, 2024). While nonperforming loans (NPLs) are a useful indicator of credit risk and asset quality, this finding implies that, at least within the parameters of this research, they might not correspond to substantial shifts in overall company performance. This means that it may not be enough for bank management to just concentrate on lowering nonperforming loans (NPLs) in order to boost ROA. It may be more productive to use a more comprehensive approach that aims to increase overall performance by improving operational efficiency, income streams, and risk management techniques.

3.7 The Moderating Role of NPL on the Impact of DPR on ROA

The data analysis showed that the impact of the Dividend Payout Ratio (DPR) on Return on Assets (ROA) is not dampened by Non-Performing Loans (NPL). This result is derived from the regression analysis, which did not reveal a statistically significant interaction term between DPR and NPL. To be more precise, the coefficient of the interaction term was -0.00 with a significance level of 0.72, suggesting that the presence of NPL did not substantially change the correlation between DPR and ROA. Statistically speaking, NPL does not serve as a moderating variable in this particular situation because it is not significant.

The results suggest that among the Indonesian banking organisations surveyed between 2019 and 2023, the effect of dividend distribution policies on company performance is unaffected by the number of non-performing loans. The relationship between dividend payout ratio (DPR) and return on assets (ROA) is positive and holds true independent of the nonperforming loan (NPL) level of the bank.

Bank management and lawmakers should take note of this finding since it implies that dividend policy measures can be pursued regardless of the extent of non-performing loans. This means that dividend policy decisions may not have to be tweaked depending on the bank's credit risk profile, which is good news for efforts to boost firm performance through distribution. Despite the fact that it does not directly mitigate the effect of the

dividend policy on performance, it is nonetheless vital for the overall financial health of banks to effectively manage nonperforming loans.

4. CONCLUSION

This study found that Return on Assets (ROA) in Indonesian banking organisations is positively correlated with the Dividend Payout Ratio (DPR), suggesting that larger dividend distributions lead to better company performance. This lends credence to the idea that greater asset utilisation and profitability might result from a dividend policy that is both well-structured and designed to boost investor confidence. While the Non-Performing Loans (NPL) ratio does attenuate the relationship between DPR and ROA, it does not directly affect ROA in a statistically significant way. This indicates that, although nonperforming loans (NPLs) are a key indicator of credit risk, they did not substantially change the effect of dividend policy on company performance over the time frame under consideration.

Several limitations are included in this investigation. First, the sample may not be representative of the banking industry as a whole because it only includes eleven businesses from 2019–2023, all of which are listed on the Indonesia Stock Exchange (IDX). The second concern is that the study uses secondary data derived from financial records, which could have reporting biases or discrepancies. Finally, the study did not take into account other possible moderating variables that may have shed light on the factors impacting company performance, such as macroeconomic conditions, managerial quality, or operational efficiency.

To further understand long-term trends and fluctuations, future studies should think about increasing the number of banking organisations included in the sample and prolonging the study period. The dynamics of banking business performance could be better understood if additional moderating variables including operational efficiencies, management practices, and macroeconomic considerations were included. More research might investigate the effects of various risks and how they interact with dividend policy in order to strengthen financial models. Finally, interviews with bank management and industry experts might be conducted as a qualitative research method to supplement the quantitative findings. This would offer practical ideas on efficiently managing dividend policy and credit risks.

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