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The Effect of Dividend Policy on Firm Value in the Era of Global Economic Uncertanty

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Abstract:

Global economic uncertainty, heightened by events such as the COVID-19 pandemic, geopolitical tensions, and volatile commodity prices, has reshaped the dynamics between dividend policy and firm value. This article review synthesizes studies published from 2020 onward that investigate how dividend payout decisions influence firm valuation across diverse industries and markets during periods of heightened uncertainty. The review highlights that while traditional dividend theories such as signalling, bird-in-hand, and agency cost hypotheses remain relevant, recent evidence suggests that market reactions to dividend changes have become more sensitive to macroeconomic volatility and investor sentiment. Many firms facing liquidity constraints opted for dividend cuts or suspensions, which often triggered negative short-term valuation effects but supported long-term resilience and investment capacity. Conversely, firms maintaining stable dividends tended to signal financial robustness, mitigating investor anxiety and enhancing firm value despite uncertain conditions. The review also identifies moderating roles of corporate governance, ownership structure, and ESG practices in shaping this relationship. By integrating these findings, the article underscores the importance for managers and policymakers to adapt dividend strategies to evolving global risks, balancing shareholder returns with financial flexibility and sustainable growth objectives.

***Keywords**: Dividend Policy, Firm Value, Global Economic Uncertainty, Investor Sentiment, Corporate Governance, Financial Resilience*

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1. Introduction

Global economic uncertainty has intensified due to crises such as the COVID-19 pandemic, geopolitical tensions, and rapid changes in monetary policies. These events have significantly influenced how firms design their financial strategies, particularly dividend policy, which has long been viewed as a key signal of corporate stability and

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long-term value. Prior research emphasizes that dividend decisions can either strengthen investor confidence or exacerbate liquidity constraints in times of volatility (Suteja et al., 2023; Rashid Khan et al., 2020). Moreover, behavioral shifts in capital markets highlight that investor psychology reacts differently to dividend announcements during uncertain periods, further linking dividend strategies to firm value (Addo et al., 2025; Abraham et al., 2023).

Dividend policy is deeply intertwined with agency theory and signalling theory, wherein stable or increasing dividends are often interpreted as indicators of robust governance and future earnings potential. However, heightened uncertainty amplifies agency costs and complicates the ability of firms to maintain consistent payouts (Seifzadeh, 2022; Burlacu et al., 2024). Studies demonstrate that ownership structure, managerial discretion, and corporate governance frameworks directly shape dividend policies and, consequently, influence firm valuation, particularly in emerging economies where investor protection remains evolving (Rashid Khan et al., 2020; Suteja et al., 2023).

Global shocks, such as exchange-rate volatility and fluctuating interest rates, further mediate the relationship between dividend policies and firm performance. Evidence from South Africa and ASEAN+4 countries reveals that global risk sentiment and monetary shifts alter firms' liquidity and capital allocation decisions (Lefatsa et al., 2025; Ogawa & Luo, 2025). These macroeconomic variables influence corporate capacity to maintain dividend consistency, thereby affecting market perception of firm stability and long-term value (Morina et al., 2020; Miloș & Miloș, 2022).

Firms facing financing constraints often adjust dividend payouts as part of broader risk-management strategies. For instance, direct tax burdens and environmental performance obligations have been found to reduce available free cash flow for dividends, reshaping investor expectations and valuations (Lu et al., 2023; Sastroredjo et al., 2025). Moreover, evidence indicates that excessive earnings management may distort dividend signals and erode the value relevance of financial statements (Burlacu et al., 2024; Hanay et al., 2024). These dynamics underscore the importance of transparent dividend policies in sustaining credibility during volatile periods.

Sustainability considerations and environmental, social, and governance (ESG) practices increasingly intersect with dividend strategies. Research demonstrates that firms investing in green transformation and low-carbon transitions must often retain greater earnings to finance innovation, potentially limiting dividends in the short term but enhancing firm value over the long run (Teng et al., 2025; Xing et al., 2025). Similarly, disclosures on tax strategies and corporate social responsibility have been shown to moderate investor reactions to dividend decisions (Shin & Choi, 2024; Silva et al., 2024), suggesting that dividend policy in the uncertainty era cannot be disentangled from broader corporate purpose.

Emerging market firms have demonstrated divergent patterns in dividend responses to crises compared to developed-market peers. Evidence from Indonesia's tax amnesty programs and cross-country corporate tax compliance studies highlights that fiscal incentives and enforcement measures significantly influence firms' retained earnings and payout behaviors (Ngelo et al., 2022; Pratama & Muhammad, 2025). These findings suggest that dividend policy during uncertain times is not merely a managerial choice but is shaped by the interplay of institutional, regulatory, and market factors (Mohammed & Tangl, 2024; Angeliki & Thomas, 2025).

Collectively, these insights reveal that dividend policy in the era of global economic uncertainty is a multidimensional construct shaped by macroeconomic forces, agency dynamics, governance quality, investor psychology, sustainability imperatives, and regulatory contexts. Understanding how these factors interact is critical for evaluating their impact on firm value across diverse market environments. By reviewing post-2020 literature, this article seeks to synthesize the evolving evidence on dividend policy–firm value linkages in a world increasingly defined by volatility and structural transformation (Charisma et al., 2025; Anton et al., 2025).

2. Methodology

This article adopts a systematic literature review (SLR) approach to synthesize empirical and conceptual studies on the relationship between dividend policy and firm value in the context of global economic uncertainty. Following established SLR protocols, the review focused on peer-reviewed journal articles published between 2020 and 2025 to capture the most recent evidence reflecting the impact of post-pandemic and geopolitical shocks on dividend practices. The selection process involved searches in multidisciplinary academic databases such as Scopus and Web of Science, using combinations of keywords including *"dividend policy," "firm value," "economic uncertainty," "tax policy,"* and *"sustainability."* Articles were screened based on inclusion criteria: (i) a clear focus on dividend policy and firm value, (ii) empirical evidence or theoretical discussion within finance and risk-management contexts, and (iii) publication in indexed journals. Excluded were studies focusing solely on technical aspects of derivatives, narrow corporate case studies without valuation analysis, or those unrelated to financial decision-making under uncertainty (Anton et al., 2025; Faedfar et al., 2022; Addo et al., 2025).

The final dataset comprised over 30 primary articles, with particular emphasis on studies examining how macroeconomic factors, fiscal policies, governance mechanisms, and sustainability practices interact with dividend decisions to shape firm value. These include research on the effects of financing constraints and environmental performance on payout capacity (Lu et al., 2023; Sastroredjo et al., 2025), the moderating role of ownership structure and governance quality (Rashid Khan et al., 2020; Seifzadeh, 2022), and the influence of investor behavior and psychological risk factors in volatile markets (Addo et al., 2025; Abraham et al., 2023). The literature was analyzed thematically, grouping findings into five dimensions: macroeconomic volatility, agency and governance dynamics, sustainability and ESG considerations, investor sentiment, and regulatory or fiscal environments. This structured synthesis enables a comprehensive understanding of how dividend policy impacts firm value amid global uncertainty, providing a robust foundation for the subsequent discussion and recommendations (Anton et al., 2025; Charisma et al., 2025).

3. Empirical Findings/Result and Discussion

Dividend Policy as a Strategic Signal during Uncertainty
Dividend policy has traditionally been perceived as a signal of financial stability, especially in volatile periods when market confidence is fragile. Recent studies underscore that stable or increasing dividends can reassure investors about a firm's profitability and governance capacity despite uncertain macroeconomic conditions (Suteja et al., 2023; Rashid Khan et al., 2020). This signalling function aligns with classical theories but has become more pronounced as global economic shocks—such as the pandemic and fluctuating interest rates—have heightened investors' demand for credible financial disclosures.

However, the literature highlights that the effectiveness of dividend signals is highly context-dependent. In emerging markets, where governance quality and investor protection are relatively weaker, stable dividends can significantly enhance firm value by mitigating agency costs (Seifzadeh, 2022; Burlacu et al., 2024). Conversely, in more developed markets with sophisticated disclosure systems, dividends are only one of several cues investors use to assess long-term performance, thereby diminishing their relative signalling power (Hanay et al., 2024).

Moreover, behavioral finance research shows that investor psychology interacts with dividend decisions under uncertainty. For example, investors often interpret dividend cuts as a sign of heightened risk even when such reductions are undertaken to preserve liquidity for future investments (Addo et al., 2025; Abraham et al., 2023). This behavioral sensitivity underscores the need for managers to communicate the rationale behind dividend adjustments to avoid misinterpretation and unnecessary valuation penalties.
Macroeconomic Volatility and Financial Constraints

Global macroeconomic volatility—such as exchange-rate fluctuations, inflationary pressures, and shifts in interest rates—directly influences firms' payout capacity. Empirical evidence from South Africa and ASEAN+4 economies suggests that global risk sentiment and monetary tightening constrain firms' liquidity, prompting them to reduce or suspend dividends during crises (Lefatsa et al., 2025; Ogawa & Luo, 2025). Such adjustments often provoke short-term declines in firm value, although they can support long-term solvency.

Financing constraints, particularly in firms exposed to heavy taxation or environmental compliance costs, further affect dividend decisions. Studies indicate that companies with higher direct tax burdens or significant obligations for low-carbon transition tend to retain earnings to fund compliance and innovation efforts, often at the expense of immediate shareholder payouts (Lu et al., 2023; Sastroredjo et al., 2025). While this reduces short-term market valuations, it may enhance long-term competitiveness and sustainability.

Additionally, evidence suggests that macro-level disruptions can amplify capital misallocation risks, particularly in firms lacking strong governance frameworks. Companies that respond to volatility with ad hoc dividend adjustments often face negative market reactions, as such behavior signals managerial uncertainty and potential mismanagement (Miloș & Miloș, 2022; Morina et al., 2020). These findings highlight the importance of integrating risk management and liquidity planning into dividend strategies during turbulent times.

Governance Quality, Ownership Structure, and Agency Costs

The interplay between corporate governance and dividend policy remains a critical determinant of firm value under uncertain conditions. Research indicates that firms with strong governance frameworks and dispersed ownership structures often rely less on dividends to signal stability because their transparency and investor protections reduce agency concerns (Rashid Khan et al., 2020; Seifzadeh, 2022). In contrast, in contexts with concentrated ownership, dividends serve as a mechanism to reduce free cash flow available for opportunistic managerial use.

Empirical studies also show that firms with active and accountable boards exhibit more consistent dividend policies that enhance valuation, particularly during crises. For example, oversight mechanisms limit the scope for earnings manipulation that could distort dividend signals and mislead investors (Burlacu et al., 2024; Hanay et al., 2024). This finding reinforces the argument that dividend policy effectiveness depends not merely on financial performance but also on governance structures that shape investor perceptions.

Furthermore, the literature highlights that cross-country differences in institutional quality shape dividend–value dynamics. Firms in emerging economies often maintain higher dividends as a substitute for weak governance institutions to assure minority shareholders, whereas firms in developed economies emphasize long-term reinvestment strategies supported by robust legal frameworks (Suteja et al., 2023; Ngelo et al., 2022). This divergence suggests that any global assessment of dividend policy effectiveness must consider variations in institutional environments.

Sustainability, ESG Commitments, and Green Transition

The rise of sustainability and ESG (environmental, social, and governance) initiatives has redefined dividend policy in uncertain times. Companies investing in green transformation often need to retain more earnings to fund innovation and capital-intensive transitions, which can limit their ability to distribute dividends (Teng et al., 2025; Xing et al., 2025). While this reduces short-term payouts, such investments are increasingly viewed as enhancing firm value by building resilience and aligning with global investor priorities.

Corporate tax strategies related to sustainability disclosures have also been found to influence dividend policies. Firms prioritizing ESG transparency often face short-term cost pressures that moderate their dividend payouts but strengthen investor trust and long-term valuations (Shin & Choi, 2024; Silva et al., 2024). This dynamic reflects a shift in investor priorities, where dividends are no longer the sole metric of value creation.

Additionally, companies operating in resource-intensive sectors experience heightened scrutiny during global economic transitions. Firms that integrate sustainability strategies into their broader corporate objectives—while maintaining clear communication about dividend adjustments—are better positioned to sustain valuation during periods of uncertainty (Sastroredjo et al., 2025; Charisma et al., 2025). This indicates that ESG commitments, when aligned with transparent dividend policies, can mitigate perceived risk and support long-term value.

Behavioral Dynamics and Investor Sentiment

Investor psychology plays a crucial mediating role in how dividend announcements impact firm valuation during volatile periods. Research highlights that risk-averse investors interpret dividend reductions as negative signals, even when firms undertake them for prudent cash-flow management (Addo et al., 2025; Abraham et al., 2023). This tendency can exacerbate market overreactions, temporarily depressing share prices.

Behavioral biases also affect investors' assessment of firms' long-term strategic adjustments. For example, studies show that shareholders often underappreciate the future benefits of dividend cuts made to support innovation, resilience, or sustainability initiatives (Zouitini et al., 2024; Katnic et al., 2024). This misalignment between investor expectations and managerial intent can create valuation discrepancies during periods of heightened uncertainty.

The literature further suggests that effective investor communication and financial literacy programs can mitigate such behavioral distortions. Firms that provide clear, timely, and credible explanations for their dividend policies are better able to align investor sentiment with long-term strategic objectives, stabilizing valuation despite short-term payout changes (Santos et al., 2025; Anton et al., 2025). These findings underscore the importance of transparency and education in managing market perceptions.

Regulatory Frameworks and Fiscal Policies

Government regulations and fiscal policies play an increasingly important role in shaping dividend policies under global economic uncertainty. Evidence from

Indonesia's tax amnesty initiatives and fiscal reforms demonstrates that regulatory incentives influence firms' retained earnings, thereby impacting dividend distribution decisions (Ngelo et al., 2022; Pratama & Muhammad, 2025). These policies can indirectly affect firm value by shaping both corporate liquidity and investor confidence.

Taxation-related perceptions also contribute to dividend policy outcomes. Studies reveal that firms operating in jurisdictions with high compliance costs often adjust their dividend strategies to balance fiscal obligations with shareholder expectations (Mohammed & Tangl, 2024; Angeliki & Thomas, 2025). As global fiscal environments become more stringent, dividend policy has become an adaptive mechanism for navigating these challenges.

Furthermore, the interaction between fiscal incentives, capital market regulations, and investor protections has been found to moderate the dividend–firm value relationship. Strong legal frameworks and well-enforced governance norms reduce the need for dividends as a substitute signal for transparency, allowing firms to reinvest earnings more efficiently during uncertain times (Saptono et al., 2024; Vezyroglou & Siokis, 2025). This suggests that regulatory contexts remain pivotal in understanding the evolving role of dividends in value creation.

4. Conclusion

This review highlights that dividend policy remains a crucial yet context-dependent factor influencing firm value during periods of global economic uncertainty. Dividend decisions serve not only as financial signals of stability and governance quality but also as strategic tools for managing liquidity and shaping investor expectations in volatile markets. While maintaining stable dividends often bolsters short-term investor confidence, well-communicated reductions or suspensions can preserve cash flow and support investments in innovation, resilience, and sustainability, which increasingly drive long-term value.

Macroeconomic volatility, regulatory frameworks, and the quality of corporate governance jointly determine how effectively dividend policies enhance firm value. Firms in markets with weaker institutional support often rely more heavily on dividends to reassure investors and reduce agency costs, whereas firms in markets with stronger legal protections and investor trust can prioritize reinvestment without significant valuation penalties. These dynamics suggest that sound fiscal policies, clear regulatory guidance, and improved transparency can help align dividend strategies with sustainable value creation.

The connection between dividend policy and firm value in uncertain environments is inherently multidimensional, shaped by behavioral responses, sustainability commitments, and shifting policy landscapes. Managers need to balance immediate shareholder payout expectations with the longer-term need to invest in innovation and operational resilience, while ensuring open and transparent communication to reduce investor overreactions. Future research should explore how crisis-driven adjustments to dividend policies affect long-term valuation and how digital transformation and fiscal changes can further influence investor sentiment and corporate payout strategies.

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