

# A Research Paper on Impact of Dividend Policy Determinants of Listed Companies on Indian Capital Market

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**Abstract** The core purpose of financial management is the maximization of shareholders' wealth with three core decisions that is, dividend, financing and investment decisions. In simple words dividend is the percentage of net profit of a company which is distributed among the shareholders. The research gap identified for this study is that, a comparison of different industries dividend policy impact on the Indian Capital Market and the samples are drawn from the National Stock Exchange (NSE) India. The main objective of this project is to study the influence of dividend policy on the market price of selected company's scrip in NSE. The researcher has chosen Empirical study to prove the hypothesis and 15 companies balance sheet for 10 years (2007-2016) were collected from the respected companies websites and the following ratios have been calculated to test the hypothesis, Net profit ratio, Gross profit ratio, Earning per share, Dividend yield, Dividend payout ratio, Return on equity and the Market price of share. The analyses conducted, the parameter estimates were viewed within AMOS graphics and displayed the standardized parameter estimates. The regression analysis model revealed that the significant impact of the independent variables on the market price of share as well as impact of dividend policy determinants on the outcome variable market price.

**Keywords:** capital structure, shareholders' equity, debt, financial ratios and share price

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## 1. Introduction

Dividend policy is a guiding principle of a company to decide the portion of its earnings and its pay out to shareholders to show weather the company goes either for pay dividend to its owners or for retaining a share out of profits to plough back in the firm or at the end of each year and it is the company's decision to how much to return to their stockholders in the form of dividends. In relation to this we talk of three types of dividends, 'the stock dividend which increases the number of share outstanding and generally reduce the price per share, 'the regular dividend which is paid in the form of regular intervals' (quarterly, semi-annually, or annually) and 'the special dividend which is paid in addition to the regular dividend.'

In addition the three main dividend policies that are used by the companies are; 'residual dividend policy', 'stability dividend policy' and 'hybrid dividend policy'. These policies are chosen by the companies based on their growth opportunities. If the company has the great opportunity to grow to retain more on the above said and it is to reduce their dividend payout rate.

In the next level of our discussion, we move on to talk about the capital market where the company can raise the capital as well as the investors can invest in the company's

capital. Share price is one of the most important components that really influence investors to purchase the shares. The share price of the companies will always show volatility because of the impacts of some factors. The dividend policy is that impacts the stock market price of the company. But the real impact on the dividend policy in stock market is still ambiguous and remains unsolved. Hence this study analyses the real relationship between the dividend policy determinants and stock market price taking into account the variables like, Net profit ratio, Gross profit ratio, Earning per share, Dividend yield, Dividend payout ratio, Return on equity and the Market price of share are used for analyzing the impact level.

## 2. Literature Review

Adnan Ali, Farzand Ali Jan and Ilyas Sharif [1] have analyzed the effect of dividend policy on stock prices. They have taken 45 non-financial companies on KSE-100 index that have earned profits and paid dividend for a period of twelve year and they used Profit after tax, Earning per share and Return on Equity as the variables. Some of findings of this study were profit retention by firms will result in a decrease in the value of the stock market prices and dividend payout have positive impact on the share prices of respected stocks.

Khaled Hussainey, Chijoke Oscar Mgbame and Aruoriwo M. Chijoke-Mgbame [16] conducted a study on “Dividend policy and share price volatility” with respect to UK stock market. The researchers used multiple regression analyses to analyze the relationship between the dependent variables and the share prices of the companies. The researchers found a positive relation between dividend yield and stock price changes, negative relation between dividend payout ratio and stock price changes and also firm's growth rate, debt level, size and earnings explain stock price changes and concluded that the dividend policy is relevant in determining share price changes.

Md. Abdullah Al- Hasan, Md. Asaduzzaman and Rashed al Karim [18] conducted a study on “The Effect of Dividend Policy on Share Price”. The study has mainly pointed at evaluating the effect of dividend policy on market price of share in the context of Bangladesh with the tools like Dividend policy, Market price per share, Earning per share Correlation and multiple regression models. The findings tell us that the effect of dividend policy on market price supports the relevant theory of dividend policy.

S.M. Tariq Zafar, D.S. Chaubey and S.M. Khalid [21] conducted a study on Dividend Policy and its Impact on the Shareholders Wealth. This study was based on the eleven selected Indian banks listed and actively traded in National Stock Exchange (NSE) during the period 2006 to 2010. The study gives an insight about the dividend and its legal implications and the relationship between shareholders wealth and the performance of the stock. The study concludes that dividend payouts have high influence on shareholders wealth and there is significant impact of dividend policy on the shareholder's wealth in banking companies in India. They were used the Multiple regression technique to analyses the data and prove the hypothesis.

Yusniliyana Yusof, Suhaiza Ismail, [25] conducted a study to investigate the determinants of the dividend policy of public listed companies in Malaysia. The variables examined in this study include earnings, cash flows, free cash flows, debt level, growth, investment, size, largest shareholders, risk and lagged dividend. The results revealed that the five factors that are earnings, debt, size, investment and largest shareholder have a significant influence on dividend policy.

### 3. Research Problem

I M Pandey (11<sup>th</sup> edition of Financial Management) evaluated the dividend policy determinants and its impact on market value of scrip. Many authors say, dividend policy has insignificant impact on the market value of the firm but the dividend policy determined based on the investment opportunities available for the company. The present study aims to find the impact of identified dividend policy determinants on the market price of the firm.

### 4. Objective of the Study

The objectives are;

- To study relationship between dividend policy determinants
- To find the impact of dividend policy determinants on the market price.
- To evaluate the dependency of dividend policy determinants on market price of various industries.

### 5. Research Methodology

The researcher has chosen the empirical study to test the impact of dividend policy determinants on Indian capital market. The present study involves a sample of 150 balance sheet and profit and loss account from three industries for the period of 2007 to 2016. The variables were empirically tested with the hierarchical regression on the companies from three industry such as pharmaceutical, Energy, and Media. Five companies from each industry were chosen thus a total of 15 companies were selected. The companies which include, Sun Pharma, Cipla, Glenmark Pharma, Dr.Reddys Laboratory, Lupin, Reliance, Gail, BPCL, ONGC, Tata Power, Network 18, Sun TV, PVR, ZEEL, and TV Today Network.

The analyses were conducted using the parameter estimates within AMOS graphics and it displayed the standardized parameter estimates. The regression analysis revealed that the factors of dividend policy such as Net profit ratio, Gross profit ratio, Earnings per share, Dividend yield, Dividend, Dividend pay-out ratio, and Return on equity influence the market price. The estimated p-value of the model can be used to test the hypothesis. If the values are significant at 5% significance level (i.e.) less than 0.05 then the alternate hypothesis are proved to be true, otherwise the null hypothesis is selected.

### 6. Analysis

In hierarchical regression, the predictor variables are entered in sets of variables according to a pre-determined order that may infer some causal or potentially mediating relationships between the predictors and the dependent variable [10]. The logic involved in hypothesizing mediating relationships is that “the independent variable influences the mediator which, in turn, influences the outcome” [14]. However, an important pre-condition for examining correlational relationships is that the independent variable is significantly associated with the dependent variable prior to testing any model for mediating variables [14].

As per the analysis, the P value of the Figure 1, shows the impact level of independent variables on dependent variables. The Gross profit (0.023) and Net profit (0.010) ratios are significant to Earnings per share as the p value is less than 0.05. Earnings per share is insignificant to Dividend yield (0.669) and Dividend payout ratio (0.884) but it is significant to Dividend (0.012) and Return on equity (0.000). The independent variables like Return on equity, Dividend pay-out ratio, Dividend, Dividend Yield ratio are highly significant to the dependent variable Market price (0.000). Here the results reveals that the dividend highly influence the market price.

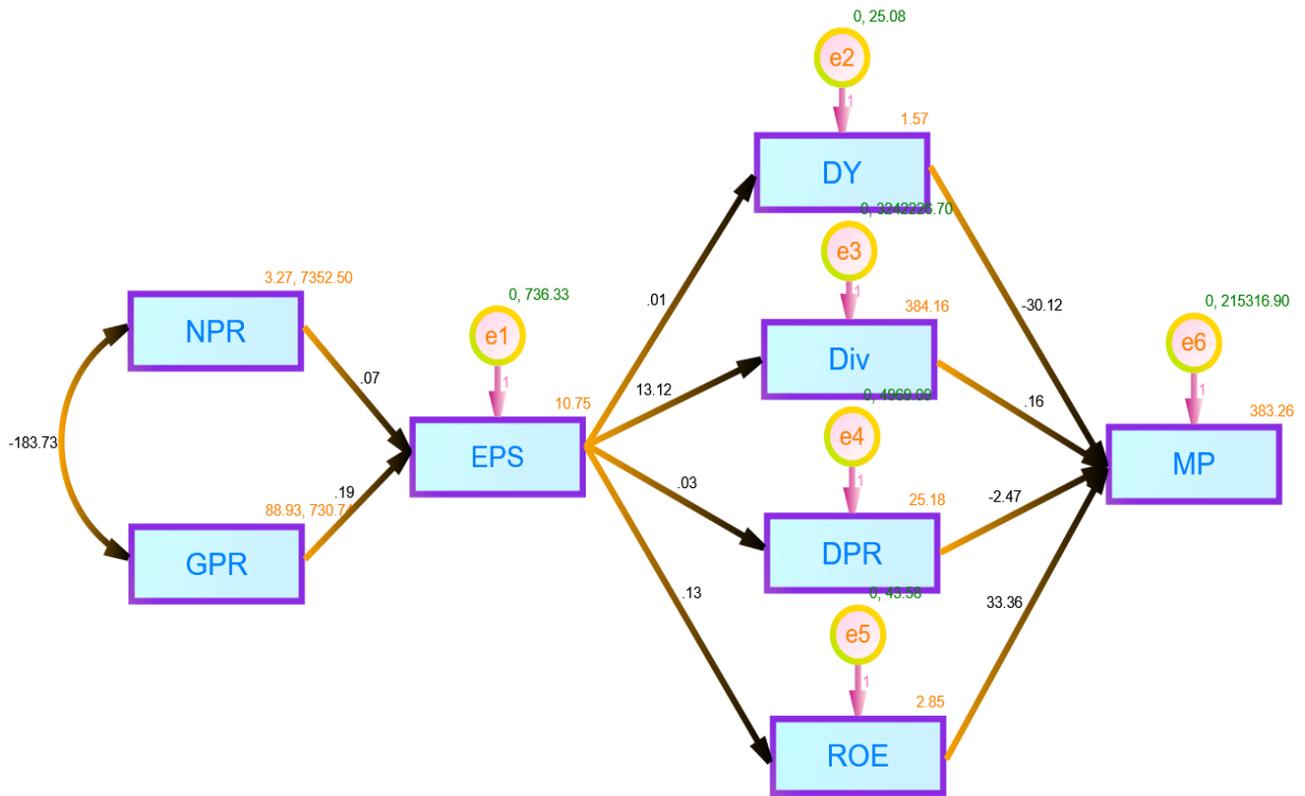


Figure 1. Structural Model – (Dividend-SEM Model)

Table 1. Regression Weights: (Default model)

			Estimate	S.E.	C.R.	P
EPS	<---	GPR	.188	.082	2.279	.023
EPS	<---	NPR	.067	.026	2.559	.010
DY	<---	EPS	.006	.015	.428	.669
Div	<---	EPS	13.119	5.248	2.500	.012
DPR	<---	EPS	.030	.205	.145	.884
ROE	<---	EPS	.128	.019	6.632	***
MP	<---	ROE	33.360	5.084	6.562	***
MP	<---	DPR	-2.470	.539	-4.580	***
MP	<---	Div	.164	.021	7.917	***
MP	<---	DY	-30.123	7.588	-3.970	***

Table 2. Standardized Regression Weights: (Default model)

			Estimate
EPS	<---	NPR	.203
EPS	<---	GPR	.181
DY	<---	EPS	.035
Div	<---	EPS	.201
DPR	<---	EPS	.012
ROE	<---	EPS	.477
MP	<---	DY	-.229
MP	<---	Div	.459
MP	<---	DPR	-.264
MP	<---	ROE	.380

Table 3. Squared Multiple Correlations: (Default model)

	Estimate
EPS	.068
ROE	.228
DPR	.000
Div	.040
DY	.001
MP	.504

The R square value shows that the overall model explaining the market is about 50.4%, the dependent variables such as Net profit ratio and Gross profit ratio is impact the Earnings per share only by 6.8% and the other factor Earning per share is explaining Return on equity by 23%, Dividend by 4% and Dividend payout ratio and Dividend yield are very meager.

Table 4. Comparison of Industry values:

PATH	Pharma	Energy	Media
EPS < --- NPR	.086	.001	***
EPS < --- GPR	.075	***	.371
Div < --- EPS	.373	.978	***
DY < --- EPS	.039	.098	.002
ROE < --- EPS	***	***	***
DPR < --- EPS	.123	.018	.070
MP < --- Div	***	.018	***
MP < --- DY	***	***	***
MP < --- ROE	.542	***	***
MP < --- DPR	***	.150	.661

The above table shows the comparison of regression analysis of the pharma, Energy, and Media industry. The Dividend and Dividend yield are highly significant to Market price and also the Earnings per share is highly significant to Return on equity with respect to all three industries. In Energy and Media the Net profit ratio is highly significant to Earnings per share, but the pharma is slightly varying (.086). Gross profit ratio to Earnings per share of Energy sector has the significance and other two industries are shown insignificant. Earnings per share to Dividend, the Media sector is highly significant and other two are insignificant. Earnings per share to Dividend yield

except Energy other two industries are significant and Earnings per share to Dividend pay-out ratio only Energy have significance and other two are insignificant. The Return on equity to Market price, except Pharma other two industries are significant and Dividend pay-out ratio to Market price only Pharma sector has significance.

## 7. Managerial Implication

According to the study, the investors should consider more on Dividend, Dividend yield, and Return on equity before they invest in securities because these variables are highly significant to Market price. The overall model shows that more than 50% R square value which is the dependent variables has a clear impact on Market price. So the investors should consider these variables before they invest in any securities for a better return.

## 8. Conclusion

Some evidence suggests that investors are not concerned with a company's dividend policy since they can sell a portion of their portfolio of equities if they want cash. This evidence is called the "dividend irrelevance theory," and it essentially indicates that an issuance of dividends should have no impact on stock price but the "relevance theory" said that the dividend policy have impact on stock price. Here the factors analyzed namely Net profit ratio, Gross profit ratio, Earnings per share, Dividend, Dividend yield, Return on equity, Dividend payout ratio to find the impact on Market price.

As mentioned early the dividend policy is the one of the factor that impacts the market price of the company in Indian Stock market. After this study researcher analyzed and proven the relevance theory that the Dividend policy determinants have a real impact on Market Price.

## 9. Scope of Future Research

The present study have chosen few companies in an industry. So the researcher can consider the entire companies for the study in an industry and also try to use the primary data.

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