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Dividend Policy

[1]K. Anuradha, [2]A.Latha
[1]Research scholar, [2]Associate professor
[1,2]Malla Reddy Engineering College (A)

Maisammaguda, Dhulapally, Kompally, Medchal, Hyderabad

Abstract: Dividend policy is a strategy used by a company to determine the amount and timing of dividend payments. The dividend decision framed by an organization or company is one of the crucial issues in corporate finance since it may have an impact on the firm's value and shareholder wealth. The research study is an attempt to analyze the effect of dividend decision on shareholder wealth. The Dividend policy has the effect of dividing its net earnings into two Parts: Retained earnings and dividends. The retained earnings provide funds to finance the long-term growth. It is the most significant source of financing a firm's investment in practice. A firm, which intends to pay dividends and also needs funds to finance its investment opportunities, will have to use external sources of finance. Dividend policy of the firm. Thus has its effect on both the long-term financing and the wealth of shareholders. The moderate view, which asserts that because of the information value of dividends, some dividends should be paid as it may have favorable affect on the value of the share. The data would be analyzed using correlation. The results of the data analysis might reveal that that there is a significant effect of dividend decision on the share price of the bank. The study is limited to a time period of 4 years.

Key words: Dividend, BSE, Shareholders wealth.

1. INTRODUCTION

An important decision of financial management is the dividend decision and the firm or company has to choose between two things:

1. Distributing profits among the Shareholders.
2. Reinvest them back in to the business.

The profits of the company or firm that remains after meeting all expenses of business, provision of taxation and depreciation and transferring the reasonable amount to the reserve funds called 'distribution profit' or 'Surplus'. A portion of this profit is distributed among the shareholders of the company or firm as dividend as the remaining balance is retained or plugging back in the business for meeting future needs of the funds and development of the company. The theory of empirical evidence about the dividend policy does not matter if we assume a real world with perfect capital markets and no taxes. The second theory of dividend policy is that there will definitely be low and high payout clients because of the differential personal taxes. The majority of the holders of this view also show that balance, there will be preponderous low payout clients because of low capital gain taxes. The third view argues that there does exist an optimum dividend policy. An optimum dividend policy is justified in terms of the information in agency costs. Meaning of dividend: The word 'Dividend' is derived from the Latin word 'Dividendum' which means 'that which is to be divided'. This distribution is made out of profits after deducting all the expenses, providing for the taxation and transferring a remaining amount to reserve from the total income of the company such distribution of profit is made as a fixed percentage o paid up capital or fixed amount per share. Thus the dividend is that portion of profit and surplus fund of the company which has been set aside by a valid act of the company for the distribution among its shareholders on record at a fixed date In proportion to their holding to be paid on demand or at fixed time. The term dividend refers to that part of the profits of a company or firm, which is to be distributed among its shareholders. It is to be defined as the return that shareholders get from the company, out of its profits, on his shareholdings in the company.

A company cannot declare dividend unless there is

1. Sufficient profits in the company
2. Recommendation of the Board of Directors
3. An Acceptance of the shareholder in the Annual General Meeting

The term Dividend refers to part of the profits of a company which is distributed among its shareholders of the company. It may also be defined as the return that a shareholder gets from the company, out of its profits, on his share holdings. "According to the Institute of Charted Accounts of India" dividend is a "Distribution to shareholder out of profits or reserves available for the purpose". The key objective is to determine the dividend policy that will maximize the market price of the shares of the firm. Dividend policy remains one of the most debatable matters in corporate finance. The best dividend policy is the one which guide to maximize of shareholder wealth and

increase the company's stock price. A dividend is the minimum return to the investors in order to compensate for the money invested and the risk taken by investing in the organization. An organization pays dividend to reward existing shareholders and to encourage potential investors to buy new issues of shares at higher prices. A dividend policy of a company may range from a decision regarding dividend action to be taken in a complex formal statement that will be approved by the board of directors and reviewed on a regular basis. Dividend policy of the firm has its effect on both the long-term financing and the wealth of shareholders.
Dividend policy determines the distribution of earnings (profits) between payments to shareholders and retained earnings. The Dividend policy in corporate finance, the decision made by the directors of a company about the amount and timing of any cash payments made to the company's stockholders. The term dividend decision plays an important part of the present day corporate world. The Dividend is an important for the firms as it may affect its capital structure and stock price. In addition, the Dividend policy determines the amount of taxation that shareholders have to pay.

Factors influencing the dividend decision

- Liquidity of funds
- Stability of earnings
- Financing policy of the firm
- Dividend policy of competitive firms
- Past dividend rates
- Debt obligation

2. OBJECTIVE OF THE STUDY

The major objective of this research is to critically analyze the possible effect of dividend policy on share prices of the public and private sector banks.

- To study the various dividend policies followed by the company.
- To analyze whether the dividend decisions have an impact on the market value of the firm's equity.

.NEED FOR THE STUDY

The principal objective is to maximize the market value of the equity shares. Hence the key question of interest to us in this study is, "What is the
Relationship between dividend policy and market price of equity shares?" Most of the discussion on dividend decision and firm value assumes that the investment decision of a firm is independent of its dividend decision. The dividend decision of a firm describes what proportion of earnings is paid to be shareholders by the way of dividends and what proportion is ploughed back in the firm for reinvestment purposes. Any firm, whether a profit making or non-profit organization has to take certain capital budgeting decision. The importance and subsequent indispensability of the capital budgeting decision has led to the importance of the dividend decisions for the firms.

IMPORTANCE OF THE STUDY

The dividend policy of a firm determines what proportion of earnings is paid to shareholders by the way of dividends and what proportion is ploughed back in the firm for reinvestment purposes. If a firm's capital budgeting decision is independent of its dividend of its dividend policy, a higher dividend payment will entail a greater dependence on external financing. On the other hand, if a firm' s capital budgeting decision is dependent on its dividend decision, a higher payment will cause shrinkage of its capital budget and vice versa. In such a case the dividend policy has a bearing on the capital budgeting decision. Any firm, whether a profit making or non-profit organization has to take certain capital budgeting decision. The importance and subsequent indispensability of the capital budgeting decision has led to the importance of the dividend policy for the firms.

3. LITERATURE REVIEW

There are number of research papers written in dividend policies earlier, which analyze relationship between dividend policies and share prices. Dividend policy has been an area of interest for a researchers in finance sense the establishment of Joint Stock Company. When a company starts generating profits, another decision may be raised: whether to distribute a portion of the earnings to the shareholders or reinvest in the business (Al-Malkawi, 2008). Dividend policy refers to the "distribution of cash to shareholders over time". As the level of equity retained in the company is affected by dividend decisions, financial managers are very careful in choosing the dividend policy. Dividend payouts influence the firm's value and most importantly, the wealth of the shareholders (Lease, John, Kayla, Lowenstein, & Sarig, 2000). Over the years, dividend policy is one of the controversial topics among financial economists- although many studies have been carried out to solve the dividend puzzle, it still remains unsolved. Due to the extensive range of debate about dividend policy, a significant amount of literature grows every day.Baker, Farrelly and Edelman (1985) in a research work survived 318 New York stock exchange firms pattern of past dividends. Pardhan (2003) after studying Nepalese firms concluded that payment of dividend have significant relationship with share prices. Nepalese shareholders prefer dividend income than long term capital gains.

- Over the years, four main topics have been addressed in dividend policy literature, i.e. the manner of determining dividend payout, the relevancy of dividends, inter-country differences in company's dividend distribution and disappearing dividends in emerging markets (Robinson, 2006).

- From the manager's point of view, the current rate of dividend payouts is usually used as a bench mark to set the dividend decision (Lintner, 1956).
- Since a change in dividend policy in a firm means a change in financial policy of that firm, there are some questions about why firms enact dividend changes,
- With some companies attempting to reduce dividends while others deciding not to pay dividends to shareholders.
- The bird in hand theory was developed by Myron Goldon (1959) and John Lintner (1962) and argues that there is a relationship between dividend payments and a firm's value. Since investors value dividends less risky compared to capital gains, firms have to set a higher dividend payout ratio to maximize the share price. In other words, high dividends increase the stock price (Robinson, 2006).
- According to Jensen (1986), there is another aspect of paying dividends baseon agency problems. When a company has free cash flow, which is excess of funds needed for positive net present value projects, then the managers would have the power and opportunity to use these funds to benefit not only shareholders but also themselves.
- Mahadwartha (2002) concluded that in Indonesia, the dividend payout is inversely related to firm size. In other words, the larger the firms in Indonesia, the less they
- Pay dividend to their shareholders. Mahadwartha reasoned that in large firms, management may take advantage of the free cash 18 flow for their interest while shareholders have less power to monitor the managers.

4. RESEARCH METHODOLOGY

A Collection of methods and methodologies that researchers apply systematically to present scientifically based knowledge about the social world. Methodology and methods, two terms are often treated as synonyms. Methodology is broader and envelops methods. It is understands the social-organizational context, philosophical assumptions ethical principles', and political issues of the enterprise (or) company of researchers who use methods.

Research: Research in a common parlance explains a search for knowledge. Once can also define research as a scientific search for pertinent information on a specific topic. In fact, research is an art of scientific investigation.

Methods: Methods are set of specific techniques for selecting cases. Measuring and observing aspects of social life. Gathering and refining data, analyzing data and reporting results.

The sources of information are classified in to two-primary data and secondary data. The data collected by the researcher and agent known to the researcher, especially to answer the research question, is known as the primary data. Studies made by others for their own purposes represent secondary data to the researcher.

Primary data: This is first hand in nature and can be collected from the company.

Secondary data

- Methods of collection of the secondary data which is already exists are Financial management text books.
- Magazines, Journals, Internet etc….

The research study is an attempt to analyze the effect of dividend policy on shareholders wealth of bank traded in Bombay Stock Exchange (BSE). This study is based on the secondary data. For the purpose of study the financial data from the period 2013 to 2016 would be used. The data would be analyzed using Statistical tool correlation. In this study market price is taken as dependent variable. Dividend payout ratio, Return on Net worth, Debt Equity ratio and total assets are used as independent variables

5. HYPOTHESES TESTING

This study focuses on examining the effect of dividend policy on share price in public and private sector banks. As per the objectives of the study the null and alternative hypotheses framed are as follows:

H0: There is no significant effect of dividend policy on share price.

H1: Dividend policy has a significant effect on share price.

6. DATA ANYLSIS AND HYPOTHESES TESTING

ICICI BANK

Year	Dividend Payout Ratio	Debt Equity Ratio	Ret On Networth	Total Asset
2013	24	10.37	1036.77	8.4
2014	24	6.30	630.26	7.8
2015	23.50	8.10	810.12	7.9
2016	28.40	9.21	920.76	7.7

INTERPRETATION: From the above information dividend payout ratio was high in 2016 with 28.40, and debt equity ratio is 10.37, return on net worth is 1036.77. And dividend payout ratio was low in 2015 with 23.50, debt equity ratio is low in 2014 with 6.30 and return on net worth is 630.26. And total assets are high in the 2013 with 8.4.

HDFC BANK

Year	Dividend Payout Ratio	Debt Equity Ratio	Ret On Networth	Total Asset
2013	19.45	841.24	1413.44	9.4
2014	19.38	1024.571	1767.02	9.2
2015	19.62	1177.943	2037.88	8.9
2016	19.53	1401.878	2431.81	9.2

INTERPRETATION: From the above information dividend payout ratio was high in 2015 with 19.62, and debt equity ratio is 1177.943, return on net worth is high in 2016 with 2431.81. And dividend payout ratio was low in 2014 with 19.38, debt equity ratio is low in 2013 with 841.24 and return on net worth is 1413.44. And total assets are high in the 2013 with 9.4.

SBI BANK

Year	Dividend Payout Ratio	Debt Equity Ratio	Ret On Networth	Total Asset
2013	19.7	2289.75	2062.04	14
2014	19.1	2400.62	1458.82	08
2015	19.4	2743.31	1754.9	07
2016	20	2910.11	1281.83	07

INTERPRETATION: From the above information dividend payout ratio was high in 2016 with 20, and debt equity ratio is high in 2015 with 2743.31, return on net worth is high in 2016 with 2062.04. And dividend payout ratio was low in 2014 with 19.1, debt equity ratio is low in 2013 with 2289.75 and return on net worth is low in 2016 with 1281.83. And total assets are high in the 2013 with 14.

BOI BANK

Year	DIVIDEND PAYOUT RATIO	DEBT EQUITY RATIO	RET ON NETWORTH	TOTAL ASSET
2013	21.6	758.585	460.805	7.6
2014	11.7	891.431	424.458	7.3
2015	19.4	929.464	256.729	7.2
2016	0	7426.879	745.048	1.2

INTERPRETATION: From the above information dividend payout ratio was high in 2013 with 21.6, and debt equity ratio is high in 2016 with 7426.879, return on net worth is 745.048. And dividend payout ratio was low in 2016 with 0, debt equity ratio is low in 2013 with 758.585 and return on net worth is low in 2015 with 256.729. And total assets are high in the 2013 with 7.6.

HYPOTHESIS TESTING:

Companies	Share price & DPO	Share price & DER	Share price & RON	Share price & TA
ICICI	-0.31534	0.961468	-0.79732	-0.54794
HDFC	0.773487	0.926691	0.920227	-0.49774
SBI	0.186616	0.377647	0.43742	-0.08156
BOI	0.991734	-0.89584	-0.77063	0.905034

7. FINDINGS

- The correlation among variables that can have impact on share price of banks. The relation of correlation matrix was obtained
- For two private sector banks and two public sector banks in india.
- In case of ICICI bank share prices is positively correlated with debt equity ratio (0.961468) which means that as there is increase in share price the debt equity ratio also increases. All other ratios shows negative correlation with share price.
- In HDFC bank share price is negatively correlated by total assets (-0.49774). Dividend payout ratio, return on net worth, debt equity ratio are positively correlated with share price means that there is increase in share price so that dividend payout ratio, return on net worth, debt equity ratio also increases.
- In SBI bank share price is negatively correlated in total assets (-0.08156) so it

shows negatively impact with share price. Dividend payout ratio, debt equity ratio, returns on net worth increases with share price because it shows positively correlation.

- And BOI bank share price was negatively correlated in debt equity ratio (-0.89584) and return on net worth (0.77063). Share price is positively correlated in dividend payout ratio (0.991734) and total asset (0.905034) so dividend payout ratio and total assets also increases because of positively correlated with share prices.

8. CONCLUSION

The above analysis and results shows a combined result. In case of correlation analysis it was found that most of the public and private sector banks show positive correlation with dividend payout ratio while some have positive correlation with debt equity ratio. As above information it was concluded that dividend policy has significant impact on share prices of banks.

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