

The Impact of Dividend Policy on Share Prices of Listed Commercial Banks in Nigeria

Lawrence Mancha Dalyop ², Robert Uma Sunday^{*}, Monday Nto Bereh^{**}

^{*}MSc Research Students, Accounting Department
Nasarawa State University, Keffi

^{**}MSc Research Student, Accounting Department
University of Jos, Nigeria

Corresponding Author Contacts:
+234(0) 0803 721 7125. lawrencedalyop@gmail.com

Abstract

Over the years, dividend policy has been one of the most widely talked about issue in the field of finance. A huge literature exists for and against the relevance of dividend policy to share pricing. Dividend relevance and dividend irrelevance schools of thought exist on this basis. While the dividend relevance school argues in favour of dividends as affecting share pricing, the dividend irrelevance school argues in favour of earnings as affecting share pricing. The current study is aimed at evaluating the relevance or otherwise of dividend policy on share pricing in Nigerian listed commercial banks. The study covers fifteen listed Nigerian Deposit Money Banks on market price of shares, dividends paid, retained earnings, and net assets for the period 2010 to 2015. Being an empirical study, it made use of the autoregressive model using econometric views (eviews) software. From the findings of the study, it is concluded that dividend policy has a significant positive effect on share valuation of listed Nigerian Deposit Money Banks. This study recommends that listed Nigerian Deposit Money Banks should ensure they regularly pay dividends to influence the market price of their shares as a way of maximizing the wealth of the owners.

Keywords: Dividend Policy, Market Price Per Share, Retained Earnings Per Share, Net Assets Per Share.

JEL Classification Codes: G35; G12; M41; M4

² Corresponding Author

The Impact of Dividend Policy on Share Prices of Listed Commercial Banks in Nigeria

INTRODUCTION

Suffice it to say that a firm's dividend policy on the current market price of its shares is a matter of considerable importance, not only to the board members, who must set the policy, but to investors planning portfolios and to other economic analyst seeking to understand and appraise the functioning of the capital markets.

Dividend policy is a major financing decision that directs the payment to shareholders a return to their investments. A firm operating in an industry is expected to follow the pattern of dividend policy employed by the industry. The demand of the firms share should be to some extent dependent on the firm's dividend policy. After the Modigliani-Miller (1961) paradigms on firms' dividend policy and their market values, there have been considerable debates, both in theoretical and empirical researches on the nature of relationship that exists between a firm's choice of dividend policy and its market value. These debates have centered their arguments on whether a 100% dividend payout ratio or 100% retention ratio or a mix of dividend payout and retention, of these three options which one is considered optimal in affecting the value of the firm and shareholders fund.

Selecting a suitable dividend policy is an important decision for the bank because flexibility to invest in future projects depends on the amount of dividends that they pay to their shareholders. If firms pay more dividends

then fewer funds will available for investment in future profitable projects. Lenders are also said to be interested in the amount of dividend that a firm declares, more money paid as dividend less money would be available to the firm to pay off their obligations. Therefore, this study will investigate the relationship between dividend policy and its impact on share valuation of Nigerian Deposit Money Banks listed on the Nigerian Stock Exchange (NSE) for the period 2010 to 2015. This is because the researcher has not come across publicly available literature on the effect of dividend policy on share valuation in relation to the listed Nigerian Deposit Money Banks that extends to 2015, which is considered very current and important, which has also used the Granger Causality test in the Vector Auto-Regression (VAR) Model. The investigation will reveal whether or not dividend policy has effect on the firms share price.

The principal objective of the study is to evaluate the effect of dividend policy on share valuation with emphasis on Nigerian Deposit Money Banks listed on the Nigerian Stock Exchange over the period 2010 to 2015 and to accomplish this, the following specific objectives are covered:

- i. To find the relationship between the dividend policy and share valuation of the listed Nigerian Deposit Money Banks.
- ii. To evaluate the dependency of share valuation on dividend per share and retained earnings of the listed Nigerian Deposit Money Banks.

To achieve the foregoing objectives, the following hypothesis was developed for testing:

H0: Dividend policy has no significant effect on share valuation listed Nigerian Deposit Money Banks.

H1: Dividend policy has significant effect on share valuation listed Nigerian Deposit Money Banks.

REVIEW OF RELATED LITERATURE

Conceptual Framework

The dividend policy of a firm determines what proportion of its earnings is paid to shareholders by way of dividends and what proportion is ploughed back in the firm for reinvestment purposes (Dalyop, 2010). Put another way, Pandey (2010), also posited that a firm's dividend policy has the effect of dividing its net earnings into two parts: retained earnings and dividends. Pandey further posits that the dividend policy of the firm affects both the long-term financing and the wealth of shareholders. The wealth of shareholders is a function of the number of ordinary shares valued at the market price at a particular date. The main objective of corporate financial management is to maximize the value of equity shares and the key point of interest is what the relationship between dividend policy and the market price of equity shares is (Dalyop, 2010). It is important to note that the amount of dividends paid to shareholders is a direct reflection of the dividend policy of the firm. This is because Pandey (2010) posited that

the firm's decision to pay dividends may be shaped by the firm's need for funds and the shareholders need for income, which encapsulates the dividend policy of the firm.

Determining share prices is a complex and conflicting task. However, economic theory agrees that the price of an asset is usually determined by the market forces (Uwuigbe, Olusegun & Godswill, 2012).

Theoretical Underpinnings

With respect to dividend policy and share prices, there are basically two schools of thought: the dividend relevance and dividend irrelevance schools (Horne, 1971; Olowe, 1998). These theories have developed relevant models to establish the relevance or irrelevance of dividend policy. These theories are often used to explain the relationship between dividend, firm performance, firm valuation, and share price.

Those within the purview of the dividend relevance school have put forward arguments that the dividend policy of a firm affects its value (or share price). Within this school of thought are the 'bird-in-hand' proponents, who argue that investors prefer cash dividends to capital gains (Amidu, 2007; Litner & Gordon, 1963); the 'tax effect theorists', who prefer lower payout companies for tax reasons (M'Rabet & Boujjat, 2016); the 'clienteles effect theorists', which explains that the preference for either high or low cash

The Impact of Dividend Policy on Share Prices of Listed Commercial Banks in Nigeria

dividend payment is dependent on the circumstances of the investor (Black & Scholes, 1974); the 'agency theorists', who argue that dividend policy is determined by agency costs arising from the divergence of ownership and control, with managers at centre of the policy, which can have a significant effect on share prices (Jensen & Meckling, 1976; Fama & Jensen, 1983) and the 'signaling theorists', who argue that managers use the change in cash dividends distributed as a means to inform investors about the company (Bhattacharya, 1979; John & William, 1985; Miller & Rock, 1985).

The dividend irrelevance theorists argue that cash dividend is not important because it has no effect on the wealth of owners. They argue that investors weigh the earnings of a firm for more than the dividend it pays, hence dividend policy has no effect on a company's value; managers will not be able to maximize the wealth of owners through dividend policy (Miller and Modigliani, 1961). This study investigates listed Nigerian Deposit Money Banks to establish the relevance or otherwise of dividend policy on their share prices.

Empirical Studies

Several studies have been conducted on dividend policy by different researchers at different periods. The correlation of price volatility and dividend yield is quite significant as compared to other variables (Asghar, Shah, Hamid & Suleiman, 2011). Dividend policy has positive influence on

stock prices (Murhadi, 2008). Dividend paying firms have a more liquid market for their stock and measures of a stock liquidity is positively linked to its probability of being a dividend payer (Igan, Paul and Pinheiro, 2010). Gittman (2004), as cited by Masum (2014) divided stock are classified into two types, such as common stock and preferred stock. He also opined that dividends are the outcome of investment.

According to Masum (2014), citing Short and Welsch (1990), a dividend is usually distributed in cash to stockholders of a corporation approved by the board of directors. It may also include stock dividend or other forms of payment. A stock dividend represents a distribution of additional shares to common stockholders. On the other hand Ross et al. (2005), as cited by Masum (2014), divided earnings into two parts; either it is retained or paid as dividend. Whereas Wild et al. (2007), Johns (1998) and Kieso et al. (2004), as cited by Masum (2014), argued that retained earnings are the primary source of dividend distribution to the stockholder. Dividends are only cash payments regularly made by corporations to their stockholders (Johns, 1998). He also specified that they are decided upon the declaration by the board of the directors and can range from zero to virtually any amount the corporation can afford to pay.

METHODOLOGY

Secondary data were used in this study. Historical panel data of fifteen listed

Nigerian Deposit Money Banks on market price of shares, dividends paid, retained earnings and net assets were collected online from the website of the Financial Times and the annual reports and accounts of the banks. Dividends paid, retained earnings and net assets were transformed into their per share equivalents by dividing the absolute figures by the respective outstanding ordinary shares of each bank at the end of each year over the period 2010 to 2015.

Model Specification

The study is an empirical study designed to utilize econometric techniques to analyze the panel data. Econometric analysis is adopted because of the involvement of economic theory, economic data and economic models in the study (Dang, 2016). The econometric technique used in this study is the autoregressive regression model computed using the econometric views (eviews) computer software version 9 to estimate the regression line.

The autoregressive model used is as stated below:

$$MPS = f(DPS, REPS, NAPS).$$

When transformed into econometric form, the model becomes

$$MPS = a_0 + a_1DPS + a_2MPS_{(-1)} + a_3REPS + a_4NAPS + U$$

Where MPS is the market price per share, the dependent variable of the research which represents share valuation; DPS is dividend per share, which stands

proxy for dividend policy, one of the independent variables of the research; REPS is retained earnings per share, the second independent variable of the research; and NAPS is net assets per share, the third independent variable of the research. $MPS_{(-1)}$, the one year lagged variable of the dependent variable (MPS) was introduced as a control variable to remove serial correlation in the residuals of the original independent variables. Also, a_0 is the intercept or constant; a_1 , a_2 , a_3 , and a_4 are the coefficients of the independent variables of the research; and U is the error term, the residual, representing other variables that may affect MPS which are not considered in the model.

The *a-priori* expectations for the model is such that DPS ; $MPS_{(-1)}$; $REPS$; and $NAPS > 0$. This means that a positive relationship is expected between the explanatory variables (DPS , $MPS_{(-1)}$, $REPS$, and $NAPS$) and the dependent variable (MPS) (M'rabet & Boujjat, 2016).

RESULTS AND DISCUSSION

Regression Results

Table 1 below indicates a coefficient of 6.567 and a probability ('p') value of 0.0000 for the intercept; a coefficient of 0.076 and a 'p' value of 0.0000 for dividend per share (DPS); a coefficient of -0.267 and a 'p' value of 0.0009 for the lagged value of the market price of shares. It also shows a coefficient of 0.012 and a 'p' value of 0.0075 for retained earnings per share, and a

The Impact of Dividend Policy on Share Prices of Listed Commercial Banks in Nigeria

coefficient of 0.001 and a 'p' value of 0.3997 for net asset per share.

The above results simply mean that both dividends and retained earnings individually have significant positive effect on the market price of shares of listed banks in Nigeria; net assets have an insignificant positive effect on market price of listed Nigerian Deposit Money Banks; while the one year lagged value of market price have a significant negative effect on market price of shares of listed banks in Nigeria.

The coefficient of determination (R-squared) of the model at 0.5114 shows that the independent variables together do have any significant effect on the market of the shares of listed banks within the sample used. This means that, collectively, variations in the independent variables of the study account for 51.14% of changes in

the market price of the shares of listed banks in Nigeria, while the other 48.86% variation in market prices of the shares is accounted for by other exogenous variables not accounted for in the model. However, the F-statistic (21.98142) with a 'p' value of 0.000000 clearly shows that the independent variables collectively have a significant effect on the market price of listed banks in Nigeria. Hossain (n.d) says in such a situation, the F-statistic takes sovereignty over the R-squared, since it relates to the population as a whole. Hence, it is taken that collectively the independent variables have significant effect on the share prices of listed banks in Nigeria. A Durbin Watson measure of 1.922932, which is close to 2.0 indicates the absence of serial correlation in the residuals of the model.

Table 1: Results of Autoregressive Model

Dependent Variable: MPS

Method: Least Squares

Date: 08/01/16 Time: 22:37

Sample (adjusted): 2 90

Included observations: 89 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	6.567892	1.237941	5.305497	0.0000
DPS	0.075837	0.014262	5.317470	0.0000
MPS(-1)	-0.267647	0.077722	-3.443630	0.0009
REPS	0.012289	0.004482	2.741658	0.0075
NAPS	0.001165	0.001376	0.846539	0.3997
R-squared	0.511417	Mean dependent var		8.398989
Adjusted R-squared	0.488151	S.D. dependent var		7.008438
S.E. of regression	5.014091	Akaike info criterion		6.116921
Sum squared resid	2111.853	Schwarz criterion		6.256732
Log likelihood	-267.2030	Hannan-Quinn criter.		6.173275
F-statistic	21.98142	Durbin-Watson stat		1.922932
Prob(F-statistic)	0.000000			

SOURCE: Author's computation using Eviews 9

To determine if the model is appropriate for carrying out the test of hypothesis, Hossain (n.d.) posits that the model must fulfill certain requirements including: (1) the model must fit well into the data through a high R-squared value (or an F-statistic that has a 'p' value that is significant; (2) the residuals of the model

must not have serial (or auto) correlation; (3) the residuals of the model must be homoskedastic; (4) the residuals of the model must be normally distributed; (5) the residuals of the model must be stationary. These requirements were tested and the results presented below.

TABLE 2: Residual Statistics

Residual Test	Type of Test	F-Statistics	Prob. (F-Statistics)	Remark
Serial Correlation Test	Breusch-Godfrey Serial Correlation LM Test	0.235101	0.7759	No Serial Correlation
Heteroskedasticity Test	Breusch-Pagan-Godfrey Heteroskedasticity Test	1.733828	0.0754	No Heteroskedasticity
Normality Test	Jarque-Bera Normality Test	4.642767	0.098138	Data is Normally Distributed

SOURCE: Author's computation using Eviews 9

Table 2 above shows the result of the test of residuals. With a 'p' value of 0.7759, which is greater than the 0.05 alpha level of significance, the result shows the residuals are not serially correlated. It also shows that the residuals are not heteroskedastic, since the 'p' value is 0.0754, which is also greater than 0.05. The residuals are also seen to be normally distributed given a

Jarque-Bera 'p' value of 0.098138, which is also greater than 0.05.

The results in Table 3 four below show that the Q-statistic with 'p' values of 0.922, 0.855, 0.929, 0.975, 0.983, and 0.350 all been greater than the 0.05 level of significance are indicative of the presence of stationarity in the residuals of the regression model.

TABLE 3: Result of Stationarity Test

Date: 08/01/16 Time: 22:59

Sample: 1 90

Included observations: 89

Q-statistic probabilities adjusted for 1 dynamic regressor

Autocorrelation	Partial Correlation	AC	PAC	Q-Stat	Prob*
. .	. .	1	0.010	0.010	0.0097 0.922
. .	. .	2	-0.057	-0.057	0.3144 0.855
. .	. .	3	-0.038	-0.037	0.4539 0.929
. .	. .	4	0.016	0.014	0.4794 0.975
. .	. .	5	0.048	0.043	0.7005 0.983
.**	.**	6	0.248	0.249	6.6973 0.350

*Probabilities may not be valid for this equation specification.

SOURCE: Author's computation using Eviews 9

The Impact of Dividend Policy on Share Prices of Listed Commercial Banks in Nigeria

CONCLUSION AND RECOMMENDATIONS

From the findings of this study, it is concluded that dividend policy has a significant positive effect on the market price of the shares of listed Nigerian Deposit Money Banks. The implication of this is that the decisions of Nigerian Deposit Money Banks to pay or not to pay dividends will affect the market prices of their shares. The following are the specific conclusions drawn from the findings:

- i. There is a significant positive relationship between dividend policy of listed Nigerian Deposit Money Banks and their share prices over the years 2010 to 2015; and
- ii. Empirical evidence shows a dependency of share valuation on dividend per share and retained earnings of listed Nigerian Deposit Money Banks over the years 2010 to 2015.

From the foregoing, this study makes the following recommendations:

- i. Listed Nigerian Deposit Money Banks should ensure they regularly pay dividends to influence the market price of their shares as a way of maximizing the wealth of the owners;
- ii. Listed Nigerian Deposit Money Banks directors should work-out robust dividend and earnings retention policies that would enhance the valuation of their businesses.

- iii. Listed Nigerian Deposit Money Banks directors should be outgoing in increasing their earnings as it can affect the valuation of their shares.

REFERENCES

- Adelegan, O.J. (2009). Price reactions to dividend announcements on the Nigerian Stock Market. AERC Research Paper 188, *African Economic Research Consortium*, Nairobi.
- Al-Hares, O., Abu-Ghazaleh, N. & Haddad, A. (2012). *Value relevance of earnings, book value and dividends in an emerging capital market: Kuwait evidence*, 23(3), 221-234.
- Al-hassan M.A., Asaduzzaman, M. & Alkarim R. (2013). *The effect of dividend policy on share price: An evaluative study*. *Journal of Economics and Finance*, 1 (4), 6-11.
- Asem, E. (2009). Dividends and price momentum. *Journal of Banking & Finance*, 33(3), 486-494.
- Braouezec, Y. & Lehalle, A. (2010). Corporate liquidity, dividend policy and default risk: Optimal financial policy and agency cost. *International Journal of Theoretical and Applied Finance*. 13(4), 537-576.
- Brandit, L.K. (1996). *Analysis for financial management*. Englewood Cliffs, N.J.: Prentice Hall.
- Dalyop, G. (2010). Fiscal deficits and the growth of domestic output in Nigeria. *Jos Journal of Economics*, 4(1), 153-173.

- Gordon, M.J. (1962). *The investment, financing, and valuation of the corporation*. Homewood, Illinois: Irwin Publishers.
- Hashemijoo, M., Ardekani, A.M. & Younesi, N. (2012). The impact of dividend policy on share price volatility in the Malaysian Stock Market. *Journal of Business Quarterly*, 4(1), 119-129.
- Hossain, S. (n.d.). *Best regression model*. Retrieved through youtube from www.sayedhossain.com.
- Igan, D., Paula, A. & Pinheiro, M. (2010). *Liquidity and dividend policy*. MPRA Paper with number 29409, University Library of Munich, Germany.
- Jais, M., Karim, B. A., Funaoka, K. & Abidin, A.Z. (2009). *Dividend announcements and stock market reaction*. University Library of Munich, Germany in its series MPRA Paper with number 19779, Posted 12.
- Jones, E.P., Mason, S.P. & Rosenfeld, E. (1985). *Contingent claims valuation of corporate liabilities: Theory and empirical tests*. In Friedman, B.M. (1985). *Capital structures in the United States*. Chicago: University of Chicago Press.
- Khan, K.I., Amir, M., Qayyum, A., Nasir, A., & Khan, M.I. (2011). Can dividend decisions affect the stock prices: A case of dividend paying companies of KSE. *International Research Journal of Finance and Economics*, 76 (1), 67-74.
- Masum, A.A. (2014). Dividend policy and its impact on stock price: A study on commercial banks listed in Dhaka Stock Exchange. *Global Disclosure of Economics and Business*, 3(1), 9-17.
- M'rabet, R. & Boujjat, W. (2016). The relationship between dividend payments and firm performance: A study of listed companies in Morocco. *European Scientific Journal*, 12(4), 469-482.
- Miller, M.H. & Modigliani, F. (1961). Dividend policy, growth and the valuation of shares. *The Journal of Business*, 34(4), 411-433.
- Murhadi, W.R., (2008). Study on dividend policy: Antecedent and its impact on share price. *Journal of Manajemen and Kewirausahaan*, 9(1), 1-29.
- Naser, K., Nuseibeh, R. & Rashed, W. (2013). *Managers' perception of dividend policy: Evidence from companies listed on Abu Dhabi Securities Exchange*. *Issues in Business Management and Economics*, 1(1), 01-12.
- Nishat, M., & Irfan, C.M. (2003). *Dividend policy and stock price volatility in Pakistan*. 11th Pacific Basin Finance, Economics and Accounting Conference.
- Pandey, I.M. (2010). *Financial management (10th edn.)*. New Delhi: Vikas Publishing House PVT Ltd.

The Impact of Dividend Policy on Share Prices of Listed Commercial Banks in Nigeria

- Rankine, GW & Stice, EK (1997). Accounting rules and the signaling properties of 20 percent stock dividends. *The Accounting Review*, 72(1), 23-46.
- Smith, (1988). Dividend policy, growth, and the valuation of shares. *The Journal of Business*, 34(4), 411-33.
- Suleman, M., Asghar, M., Ali Shah, S. & Hamid, K. (2011). *Impact of dividend policy on stock price risk: Empirical evidence from Equity Market of Pakistan*. The Dhaka Stock Exchange (2013). Viewed 25 March 2013 from <http://www.dsebd.org>.
- Uwuigbe, U., Jafaru, J. & Ajayi, A. (2012). Dividend policy and firm performance: A study of listed firms in Nigeria. *Journal of Accounting and Management Information Systems*, 11(3), 442-454.
- Uwuigbe, U., Olusegun, O. & Godswill, A. (2012). An assessment of the determinants of share price in Nigeria: A study of selected listed firms. *ACTA Universitatis Danubius*, 8(6), 78-88.
- Van-Horne, J.C. (1979). Optimal initiation of bankruptcy by debt holders. *The Journal of Finance*, 3(3), 897-910.
- Weston, J.F. & Brigham, E.F. (1972). *Managerial finance*. 4th Ed. New York: Holt, Rinehart & Winston.
- World Bank (1996). *Implementing the World Bank's gender policies: Progress Report No. 1*. Washington, DC: World Bank.