ISSN: 2456–5474 RNI No.UPBIL/2016/68367 Vol.-6* Issue-10*November- 2021
Innovation The Research Concept

The Effect of Dividend Policy on Share Price:A Conceptual Review

Paper Submission: 10/11/2021, Date of Acceptance: 23/11/2021, Date of Publication: 24/11//2021

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Abstract

In today's industrialized world and the world with all kinds of technology there is still no response to the equity policy and so far the equity policy is remembering a potentially controversial topic in business finance. Because of the complexities associated with the impact of profit policy on stock market value, books on this topic have grown rapidly over the past few decades. Current research conducts randomized reviews of textbooks on practical subjects and theory of corporate share policy so that we know and understand its nature and magnitude. In this case, an in-depth review of previously conducted research has been conducted and it is evident that there are different types of methods or school of thought related to share policy. The first school of thought suggests that the increase in share payments will increase the firm, while the second is completely contrary to the first and suggests that the increase in share policy will reduce the value of the firm. The third supports Miller and Modigliani (1)'s argument that a fixed share price is not affected by the equity policy. So far no standard results have been obtained which is why the results are not clear. This article also attempts to cover important international policy studies, showing that the outcome of a share policy differs from country to country. Contextual content and a wide range of discussions about the effect of stock market pricing policy have made a huge number of books growing every day. Therefore, it is not possible to make a complete review of all the arguments.

Keywords: Dividend policy, share price, fixed price, Dividend policy ideas.

Introduction

The stock policy has always been a matter of great concern to them and there is an ongoing debate on this issue from studies conducted by Lintner and Gordon. As a share policy is one of the most notorious or complex issues and a major financial aspect of a business. This is an important topic not only because of the large amount of money involved, but also because of the recurring nature of share payments. The share payment policy is closely related to the company's investment policy and other financial laws. Following the discovery of the MM theory of profit margins, a number of studies have been conducted in the field of share payment decisions worldwide. Dividend rhetoric theory assumes that in a well-functioning and complete market where there is no equal knowledge or taxes and operating costs, a company's dividend policy has no effect on its market value which is reflected in the company's share price and the company does not have 'effective equity policy. Although in a good market where an investor can get all the information quickly for free and no transaction costs or taxes included are far from the distance. On the other hand, theory has shown that investment is important and is a key issue for any company. The structure, proposed by MM is the basic enemy of all studies that have been done generally with the share payment policy. Allen and Michaely also argued that their formation was so sufficient that it included both repurchase and shares, while the company's value was determined by the company's investment strategy. It is thought that the company's main goal is to increase the wealth of shareholders, but according to Block and Hirt; this idea is not simple as the price of shares is directly influenced by the corporate management body but there is only one way in which the company's pricing can act in accordance with the corporate investor's intentions. Barman states that "if dividends are a major indicator of stock prices and stock prices are a major indicator of the value of firms, it is important that in order to increase shareholding wealth, a company must adopt a share price policy that will increase stock prices". The shareholder's asset is therefore recognized as the sum of the company's ordinary shares which are considered to be the present value of the present cash to be paid to the existing shareholder and the required rate of return is used for the discount. This cash flow includes cash appreciation and dividend. Therefore, companies must make an important

decision about the amount of the fund company that they must keep in order to grow and distribute the profit to their existing shareholder, and the decision should be made as to how the dividend should be given most of the time dividend distribution. There are various ways in which a cash dividend can be paid (annual or semi-annual) or declared bonus shares.

The main purpose of this paper is to provide a summary book review that focuses on the effect of stock policy on stock prices by reviewing existing theories related to stock policy and its intended outcomes. This paper also examines the research that has been done to find the link between equity policy and stock prices in countries. This research based on small research has contributed to the field of stock policy literature.

Objective of the Study

The objectives of the study are following:

1. To know the different theories and types of dividend policy adopted by companies.
2. To analyse the impact of dividend policy on share price of the company.
3. To study the different dividend policies used by countries while declaring dividends.

Why Companies Pay Dividend

In finance, most studies focus and focus on the equity policy. Many writers and researchers have defined the concept of dividend, as it is a return on investment for the investor or fund and the trust in the company. According to Bierman, a dividend is usually a dividend that is distributed to shareholders after deducting fixed interest rates and a tax liability on the profits earned by the company. Dividend is therefore a tax levied on shareholders and there is no need to pay tax on the proceeds. This concept is very much in line with the views of Watson and the Head. However, the dividend can still be distributed to shareholders in three ways; namely cash, stock and liquidation dividend. Additionally, Jo and Pan argued that dividend payments could give investors an impression that the company meets the requirements for good business management practices. According to Lease, John, the company's dividend reflects the "practice that managers follow in making dividend payment decisions or in other words, the dividend pattern and the size of the distribution over time to shareholders". Since 1950, the attention of professors of finance has been the focus of corporate share policy decisions. A lot of research has been done to solve the profit problem for decades, but the widely accepted coverage of the expected payment behavior of a payment company has ever been disclosed or made public. Myers says the share payment policy is among the most unresolved issues in the financial economy. This fact is similar to Black who finds that "the more closely the payment policy is, the more difficult it seems, as it has the unrelated components". The study calls the dividend policy a "dividend puzzle". Since the release of Black, a large amount of research has been done to solve the dividend puzzle problem. Allen, Bernardo elaborated on the existing consensus view that "Although a few theories have been put forward in the literature to explain their ubiquitous existence, profits remain one of the major issues in business finance". It corresponds even to a particular idea or feature. Thus, a combination of belief occurs about the fact that companies pay dividends and that the choice of a particular dividend policy can affect stock prices and strong value.

Theories of Dividend Policy

Shared policy remains an unresolved topic and unresolved mystery in the business finance environment. Several studies had already been conducted on the dividend policy, leading to a solid foundation of controversy in the financial sector. The financial books contain various supporting ideas such as budget irregularities, compliance, bird hand, signals, agency and customer outcome. Brealey, Myers said the budget increase reflects management's confidence in profits and therefore affects the company's share price. However share price increases and unexpected profit increases are only possible if information related to future benefits is disseminated through other channels. The question arises as to whether the dividend only provides a signal of a stock price or the dividend influences the stock price or the market value of the firm. These aspects are discussed in more detail with the help of various share policy ideas in the following sections:

Dividend Irrelevance Theory

Miller and Modigliani proposed one of the most influential and influential aviation projects. Although, it was introduced more than fifty years ago but so far its legitimacy still lies in the decision-making process of the company and is considered one of the most widely followed ideas. When the disrespectful proposal is published in the article “Shares Policy, Growth and Stock Equity”, it alters the beliefs of both academics and employees about profit and introduces a new foundation for them. Prior to the proposal of the disrespectful theory of MM, the common belief was that dividend pay was in line with corporate value. This idea comes from Krishman's view of the "Bird-in-Hand" hypothesis. Both ideas were contradicted in their work that "the sole purpose of the company's existence is to pay dividends and high-paying firms must sell their shares at high prices" as quoted by Frankfurther, Kosedag.

However, at the beginning of the financial period, Miller and Modigliani introduced the irrelevance theorem, more commonly known as the MM theorem. They argue that under certain assumptions, a company's profit policy does not affect the share price or capital cost; if the policy in divisions does not have significant implications, it will not work. The basic premise of their argument was that the value of a company is determined by its ability to profit and depends on its profitability by choosing the right investment policy. Therefore, when an investment decision is made, the payment policy becomes an insignificant factor in the value of the company. This is because the difference between the investment and the receivable, and the balance represents the total amount of the payment. In other words, the value of a company depends on the revenue received by its assets and not on how revenue is divided into retained profits and dividends. From an investor's point of view, the profit margin is useless, because fair buy and equity sales can double the desired payments. The Company may change its profits to any level with the corresponding change of its remaining share. According to the authors, the dividend policy is not in line with the shareholder, as it will not change the wealth of the shareholders; therefore, any dividend policy investors will not pay its premium. This suggestion comes with some thought. In the midst of this consideration the opponents of this theory look at a few in realities. Dividend irrelevance theory has five main ideas. First of all, the information is symmetrical and free (inexpensive) is equally available to everyone in the market. Secondly there are no business taxes on capital gains and dividends. Third, the cost of transportation and floating is not limited to the purchase and sale of securities. Second, there is no difference between management and security manager interest i.e. there is no agency cost. Fifth, individual firms and investors are unable to influence the price of collateral in the market. Among these assumptions, the practical value of a few speculations is lacking. For example, there are many researchers who are already opposed to the idea that there is no agency problem. Opponents of this proposal argue that the company has the same management and ownership which means that the manager will act in a way that benefits his or her shareholder. This argument is also supported by Nizar Al-Malkawi, who explains that agents or managers will follow those policies of their own interest in the cost of company owners. Much of the waste has already been done on the grounds that it is tax-free, as it does not apply at all in today's world.

Dividend Relevance Theory

Research by Baker and Powell discusses how executives think an effective way to increase the number of investors can be by paying dividends and that higher dividend policy should be an equal combination of future growth and profit margins. These findings also support the Linter study which argues that shares are an important part of a strong value. In Gordon's view, dividend plays an important role because it has been used in his research as a means of measuring companies.

However, investors may view dividend policy as irrelevant but emperically; shares have proven to be valuable in the eyes of investors. In a world of uncertainty and uncertainties, investors can be affected by a profit policy by considering the behavior and imperfections of the markets. This is a market bias "the result of a bird in the hand". They discussed the problems company executives face when choosing a dividend approach and explained why investors consider dividend policy as a priority by applying four distinct and relevant facts.

Bird-in-hand Theory

The opposite view of MM's theory of disrespect is that the company's value can be influenced by profits and this proposal is described as "bird theory". Linter introduced this idea for the first time and became the basic term for all those studies that say company value is closely related to share payments. This idea is developed with the idea “Better a bird in the hand than two in the forest”. This view suggests that investors' preferences are "one bird in the hand" representing the distribution of the dividend from stock, because it is "better than two in the woods" with a monetary gain that can be high and uncertain. In monetary terms, investors are more likely to invest in stocks that offer current shares than those that issue future shares and retain profits. This view was further supported by Gordon. He said investors are interested in their repayment and prefer to receive shares today because of the high level of uncertainty that exists in profitability and future shares. This view is also supported by Nizar Al-Malkawi, who says investors are looking at shares with a higher value than stocks saved due to uncertainty about future cash flows. Current profits are more certain than financial gains because managers do not control the price of stocks but rather market forces due to the high level of uncertainty involved. The strongest reason for this is that investors are willing to protect a certain amount of investment as investments hold a level of uncertainty.

Bird in hand theory suggests that obtaining a dividend of money now could eliminate the risks associated with uncertainty over deferred income or greater profits. Therefore, investors will be more interested in buying shares of companies that pay continuous shares than those companies, which save a lot to grow and expand. According to Khan and Jain, the basic ideas of the Gordon model are based on the idea of exploring among the potential benefits of the future. The implication of this is that if the future is more complex then there is a chance of uncertainty about future profits but there is no security about the investor who will get a better return because of the high level of uncertainty. Therefore, investors will not be interested in investing in firms where shares are very distant. always. Although firms do not pay the current dividend, investors will use the maximum discount rate to reduce the profits of these companies, thus the value will be lower compared to current companies paying dividends.

As discussed above that this theory contradicts MM's dividend irrelevance theory and states that high-profile companies pay more shares to their shareholders. As this view conflicts with MM theory, it can be considered offensive to explore the notion that highly profitable firms offer additional benefits to their shareholders. If the company makes enough profit then the investor may look at the potential, but if the company does not make a big profit then the opposite may be true.

Signaling Theory

In the free market, all related stakeholders have the same company information that includes shareholders, bankers, executives and others. However, if one participant has more information about the company’s future forums and current conditions than other participants there is a state of information disparity.

The concept of knowledge asymmetry was introduced by Akerlof, who explored the market for "lemons" with the help of automobile markets. In the presence of information asymmetry, all items (lemons suppress bad cars and cherries mean good cars) on the market can be sold at the same price because owners can only distinguish the feature of cars. Therefore, under the condition of knowledge asymmetry, the owner of a good car will try to show good information to outsiders. Similarly, companies that distribute shares can be seen as a sign of good hope for the future and are not like “lemons”. The theory of signing shares has its roots in a study presented by Linter who revealed that a company’s stock price often fluctuates with the shareholders ’change. Although Miller and Modigliani have said they support the theory of budget deficit, they also argue that in the real world to ignore flawed financial markets, the benefits are linked to “information content” that could affect the stock market value. Since then many researchers have been part of the process of developing this theory and today it is considered one of the most important dividend theories.

Signaling theory is one of those ideas that consider dividends to be important in affecting the value of a company. While Miller and Modigliani thought that managers and investors knew the exact situation or information about the company. This proposal has received a lot of criticism. As several researchers believe that the managers involved in managing the company's day-to-day operations have more accurate and timely information about the company compared to foreign investors. This creates a gap between investors and managers. To close this information gap, Nizar Al-Malkawi says shares could be used as one of the ways for managers to communicate confidential information to shareholders. However, the increase in profits can be understood as good knowledge and bright prospects.

Agency theory

The hypothesis given by Jensen and Meckling is seen as a benchmark for agency theory. They argue that when managers are given the responsibility and responsibility to increase the wealth of shareholders, a conflict of interest begins between shareholders and managers. This idea was also discussed by Ross. This disagreement arises when executives act in such a way that their wealth increases at the expense of the principals who actually own the company. This argument contradicts the proposals of Miller and Modigliani who expected the managers to be perfect employees on behalf of the principals and there was no conflict of interest in them. This is a dubious idea that shareholders are different companies from company executives. Therefore in such a case, the intentions of the trustees are not necessarily the same as the intentions of the shareholders and the trustee may perform more expensive and risky activities in the interests of the shareholders i.e. using excessive compensation or investing in those projects that provide unnecessary return to them. they are of no benefit to shareholders. Therefore, shareholders should bear these costs required to monitor the conduct of management. These costs are significant and may be the result of an inconsistent profitability between shareholders and company executives. Therefore, share payments are a way of arranging conflicting positions and resolving ownership issues that arise between shareholders and executives, by limiting the amount remaining in the management judgment. Therefore, the shareholder can check the management economically. Thus, it shows that paying dividends can reduce the chances of managers doing things selfishly because interest payments increase the accountability and accountability of managers to a few participants.

Clientele effects of dividend theory

This perspective dictates that different investors or shareholders have their own expectations and choices about share payment policy. As a result, shareholders often choose stock firms that suit their particular needs. This is because shareholders have to deal with different tax management in order to maximize profits and dividends and face certain operating costs as they buy or sell securities in different markets. Miller and Modigliani found that in order to reduce these costs, shareholders would have to go to companies that offered the expected shareholders' profits. At the same time companies will want different customers established in their share payment policies. However, they argue that while a customer outcome may change a company’s share payment policy, one customer is just as important as the other, thus a share payment policy remains unimportant. Nizar Al-Malkawi thinks that companies in their development phase, who want to pay smaller dividends will attract customers to apply for a bigger loan, similarly those companies in their maturity phase will distribute a large dividend to customers who need immediate income in the form of dividend. There are two customer outcome groups, those based on tax and transaction costs. The study states that investors in high tax areas will attract those stocks with less or no share in compensation in the form of higher stock prices and vice versa. Berk and DeMarzo explained that individual investors in a market with 54% of the stock market value would receive only 35% of profits. On the other hand the cost of transactions involving customers occurs when small investors rely on different currencies for their need because they cannot keep up with the high operating costs that include selling securities. All investors should deal with these outcomes differently, depending on the size of the portfolio and the type of investor and where the buying and selling of securities is done.

Research Method

This study is basically a conceptual review paper that examines the impact of profit policy on stock prices by reviewing existing ideas related to equity policy and its validation in different countries. Carrying out the review process involves the different stages as shown in Figure 1. We have searched different websites (Google Scholar, Web of science and EBSCOhost), which are used extensively by the researcher in a number of fields. As the share policy is widely discussed in corporate finance, we therefore have very little difficulty in finding related articles. In the process of reviewing these articles, we also found related references, which made our search for literature easier. During the literature search, we also identified several financial blogs on stock policy and its impact on market value, which are also relevant to our research. But we do not include these blogs because they are considered to be unreliable and biased and only true resources were used in study.

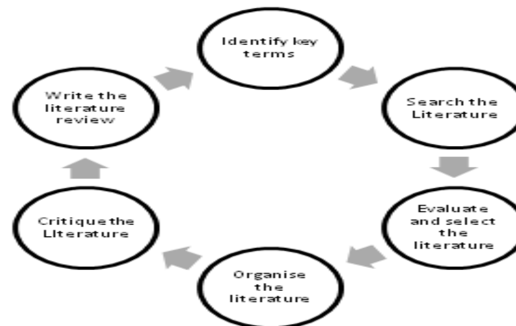

Figure 1: Literature Review Process

Empirical evidence from different countries

Extensive empirical research has been conducted to analyze the relationship between stock policy and stock price. However, these researchers have no consistent findings. Black and Scholes found that there is no correlation between stock prices and equity policy which also explains that it is an investment decision for investors to hold low or high return securities and in both cases the return earned remains the same. According to Baskins, there is a negative correlation between dividend yield and stock prices. However, the findings of the study did not agree with Hussaney, Oscar Mgbame. Many different researchers have found strong evidence that it supports MM irrelevance theory of dividend and do not believe it is related to the number of assignments..

Gordon introduced another concept about budget policy which is a relevance theory of dividend. The theory is that the share payment policy affects the market value of stocks and the value of a company. Investors are likely to earn a safe and current income in terms of dividends rather than higher profits. The concept was also supported by various studies conducted by Baker and Powell, Myers and Frank.

In developed countries, the relationship between policy dividend and the share price is well researched and research is done regularly. Looking at the US market, the market shows a positive correlation between interest rate and shares by Asquith and Mullin Jr. The findings of this study were consistent with Ariff and Finn, Conroy, Eades which were conducted in various developed countries. But in the event of a study by Bulan, the Subramanian found a negative and positive relationship between stock policy and stock price. However, there is no relationship between the share policy and the number of shares that Iqbal and Rahman represent in developed countries. In the case of developing countries, most studies have shown a positive relationship between monetary policy and stock prices. This study contradicts the research of Mahdavi and Ardekani, Shah and Noreen, Hunzra Ijaz as they found both positive and negative relationships between profit policy and share capital. There are also a few studies that do not find a relationship between share policy and share price in the case of developing countries.

Conclusion

The share policy has been one of the most widely discussed topics and one of the most unresolved issues in the area of business finance. Many studies had already been done on the dividend policy, leading to a strong bone of contention in the financial sector. The question arises as to whether the budget policy affects the value of the budget or not is still allowed to discuss politics among policy makers, managers and researchers to date. From the textbooks, the stock policy can be divided into two groups, the non-essential school of thought given by Miller and Modigliani, who says the stock market policy and stock price mean nothing while the second school of thought supports Gordon's theory and believes corporate dividend. policy affects the value of shares. Therefore, the problem that exists between a manager and an investor is the theory that a company should use when making stock decisions. Although various studies have been conducted on various issues related to equity policy, namely why firms pay dividends, but the dividend puzzle remains unresolved and has yet to come to fruition. The eperical literature has seen a systematic deviation from the share policy pattern in different companies, and in different countries at different times. It builds on the theories of the past fifty years and all the evidence does not provide a solid conclusion and does not specify the effect of a policy on profit in stocks. Also, our review findings have norworth policy implications for academic students, analysts, administrators, speculators and investors. These company executives can assess the effect of a share policy on the number of shares in various sectors of the economy

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