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DIVIDEND POLICY AND MARKET PRICE OF SELECTED LISTED FIRMS IN NIGERIA

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ABSTRACT

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Dividend policy plays a major role in maximization of shareholders wealth. The objective of this paper is to investigate how dividend policy of a company affects market price per share. Secondary data was obtained from the Nigerian Stock Exchange and annual financial statements of selected companies. The study employed ordinary least square (OLS) regression technique using e-view software to establish the relationships between the variables dividend policy and stock prices of the selected companies. The findings aligned with the Lintner's (1956) findings that decrease in or non-payment of dividend could convey wrong signals to investors.

KEYWORDS: *Dividend policy, Nigerian Stock Exchange, firms, financing decision*

1.0 INTRODUCTION

One of the most important roles of financial managers is that of determining how much of the firm's earnings should be allocated between retained earnings and dividend. Dividend is the return that accrues to shareholders as a result of the money invested in acquiring share in the stock of a given company. When a company makes a profit, the company's board of directors will need to determine the level of the profit that is to be paid as dividend to equity holders and the form the dividend is to take. The basic issue is whether dividend should be paid now or plough back for business growth. The role of the financial manager therefore is to strike a balance between dividend payout and retention of earnings. This is a very difficult task because shareholders have different and conflicting objectives. Some shareholders will prefer steady flow of income while others will prefer capital gains arising from increased share prices. Companies and Allied Matters Act 1990 stipulates that dividends cannot be paid out of capital since this will lead to a reduction of the company's capital which is against the legal principle that the capital of the company must be maintained. CAMA stated further that dividend should not be paid by the company if it will make it unable to pay its debt as and when they fall due.

Dividend policy is concerned with division of net profit after taxes between payments to shareholders (ordinary shareholders) and retention for reinvestment on behalf of the shareholders (Adediran & Alade, 2013). Various firm's adopt dividend policies depending on the company's articles of association and the prevailing economic situation. Some make high pay out, while others make low pay out and yet other pay stock dividends (bonus issue) in lieu of or in addition to cash dividend while others pay cash only.

According to Owualah (2003), the dividend policy of firms is influenced by many factors ranging from legal constraints, contractual factors, internal factors in term of cash from internally generated operation and investment opportunities and prospects of the companies. Other factors enumerated are: owners' consideration with respect to the maximization of their wealth in the long run; the prevailing income policy of a government i.e where government policy stipulates the maximum percentage of profit after tax that can be paid as dividend and finally, the prevailing dividend practice in a firm's industry could also influence its dividend policy. The optimal dividend policy of a firm depends on investor's desire for capital gain as opposed to income, their willingness to forgo dividend now for future returns, and their perception of the risk associated with postponement of returns. The

goal of the corporate entities is to maximize the value of the shareholders investment in the firm. Managers pursue this goal through their investment, financing and dividend decisions. Investment decision involves with the selection of project with positive net present value while financing decision involves with selection of capital structure that would minimize the cost of capital of the firm (Ali & Chowdbury, 2010). In addition, managers need to decide dividend decision on a regular basis that involves with whether to pay earnings to shareholders to reduce agency problem (Jensen & Meckling, 1976).

In any country, capital market is considered to be very attractive place for investment opportunities. In the case of Nigeria, capital market investment is very important and significant for the development and market capitalization of domestic industry, trade and commerce. Capital market according to literature always complements the effort of the banking sector by mobilizing financial resources for long-term investments. Many profitable investments require a long-term commitment of capital and investors are reluctant to relinquish control of their savings for long period (Ologunwa & Sadibo, 2016). Investors in capital market consider several things before they invest their funds in any particular securities. Among them, so far the most important subject matter is return from investment in securities that partly depends on dividend announcement in the stock market. On the other hand, announcement of dividend is considered to be a significant variable for stock price movement (Ali & Chowdbury, 2010). If the value of a company is a function of its dividend payments, dividend policy will affect directly the firm's cost of capital. Dividend policy has been analyzed for many decades but no universally accepted explanation for companies observed dividend behavior has been established (Samuel & Edward, 2011).

In Nigeria, different studies have come up with different results, it is for this reason, this study seeks to investigate relationship between dividend policy and market price of listed companies in Nigeria.

2.0 LITERATURE REVIEW

2.1. Conceptual Issues

Importance of dividend in the business world cannot be over-emphasized. A number of shareholders, investors, managers lenders, financial consultants/analysts use it in making informed decisions. Considering the importance of dividend from the investors' point of view, dividend is not only a source of income but also a way to assess a company from the investment point of view. In other words, the main objective of investing in the stock market is to maximize the expected return at low level of risk, and this return may be in the form of dividend or capital gain. In effect, maximizing shareholders wealth depends on the dividend policy of the company (Khan, 2012).

Pandey (2011) defines dividend as that portion of a company's net earnings which the directors recommend to be paid to the shareholders in proportion to their shareholdings in the company. It is usually expressed as a percentage of nominal value of the company's ordinary share capital or a fixed amount per share.

Dividend policy suggests a positive attitude for it is a deliberate policy to maintain or increase dividend at a certain level with the ultimate aim of sustaining the price of the ordinary shares on the stock exchange. This is because capital markets are not perfect, although shareholders are indifferent between dividend and retained earnings due to market imperfections and uncertainty, but they give a higher value to the current year dividend than the future dividend and capital gain. Thus, the payment of dividend has a strong influence on the market price of the shares. Management might maintain a dividend level even at the expense of liquidity or forced into borrowing to do so. With this approach, it holds that dividends on the other hand are desirable from the shareholders point of view, as increasing their current wealth and consequently, dividend level determines share price as well as indicates the prospects of profitability of the firm.

On the other hand, profit retention policy tends to suggest a more passive residual attitude towards dividend, that is, a positive attitude towards retention. Dividend payout reduces the amount of earnings to be retained in the firm and affects the total amount of internal financing. When dividends are treated as a financing decision, the net earnings of the firm may be viewed as a significant source of financing the growth of the firm. Dividends paid to shareholders represent a distribution of earnings that cannot be profitably reinvested by the firm. The approach to dividend is viewed merely as a residual decision. This theory is known as the residual theory of dividend and was first proposed by Modigliani and Miller in 1961. Investors prefer to have the firm retain and reinvest earnings rather than pay them out in dividend.

2.2 Theoretical Frameworks

Akinsulire (2015) stated that there are two (2) theories of dividend policy:

The Dividend Irrelevancy Theory and

The Dividend Supremacy/Relevancy Theory

The Dividend Irrelevancy Theory: In 1961 Franco Modigliani and Melton H. Miller (M-M) argued against the claim that an active dividend policy should be pursued as a means of maximizing shareholders wealth. They argued that in a tax-free world, shareholders are indifferent between dividend and capital gains and the value of a company is determined solely by the earnings power of its assets and investments.

M-M theory is anchored on the following assumptions: perfect capital markets where investors act rationally and have access to perfect and costless information; no floatation costs on securities issued by a company, and so transaction cost on securities sold by a shareholder; a world of no taxation, or if there is taxation, the same tax rate is applicable to capital gain and dividend income; perfect certainty by every investor as to future investments and profits of the company, risks of uncertainty do not exist and the company will maintain a fixed investment policy.

Modigliani and Miller assumptions have been criticized on the ground that; there exists imperfect capital market; there exists transaction costs and floatation cost; there exist taxes and tax rate applicable to dividend may be different from that of capital gains; there may not be a fixed investment policy and that the basic desire of an investor may be to obtain current income and to have diversification of portfolio.

Another school of thought on dividend theory is the Dividend Supremacy/Relevancy Theory. The proponents of theory especially Professor James Walter and Gordon (1959) argued that dividends were all that mattered in the determination of share prices. This is based on the fundamental theory of share values. It is based on the assumptions that: the market value of a company's share depends on; the size of dividend paid; the growth rate in dividend and the

shareholders' required rate of return. Others are: the growth rate in dividends depends on how money reinvested in the company, and so on, the rate of earnings retention; and how shareholders will want their company to pursue a retention policy that maximizes the value of their shares.

2.3 Empirical Evidences

From the empirical evidences are the following results:

Uddin and Chowdbury (2005) in their study, selected 137 companies which were listed on Dhaka Stock Exchange (DSE) and studied the relationship between share price and dividend payout. The results showed that dividend announcement does not provide value gain for investors and shareholder experience approximately 20% loss of value during thirty days before the announcement of dividend to thirty days following the announcement. Their finding supported the irrelevancy of dividend policy. In a study by Muhadi (2007) on the impact of dividend policy on share price in the Indonesian capital market based on the signaling theory using a multiple regression model of data gathered from a sample of 84 companies from 142 consumer product companies listed in the main market of Bursa Malaysia for a period of six (6) years from 2005 to 2010. The empirical results of this study showed significant negative relationship between share price volatility with two main measurements of dividend policy which are dividend yield and dividend payout.

Khan (2012) conducted research on the effects of dividend on stock prices and a data sample of twenty-nine companies was taken covering the period 2001 to 2010. Fixed and random effect models were applied on the panel data collected. The result showed that a significant positive relation between dividend, earnings per share and profit after tax to stock market prices.

Adeyemi and Adewale (2004) evaluated the dividend practices among selected Nigerian quoted firms. Survey method was adopted in the study and a structured questionnaire was employed. The result of the survey questionnaires showed that Nigerian investors' attitudes are consistent with those of the bird-in-hand theory and that Nigerian managers belief that dividend payout have significant signaling effect both on share price and future prospects of a firm.

Adesola and Okwong (2009), in a similar study made an attempt to evaluate the observed dividend policy of a cross section of 27 Nigerian quoted companies using theories tested to explain dividend behavior of those firms. Data covering the period 1996 to 2006 were reviewed and a model with necessary policy variable was constructed. Their study revealed that the traditional factors are significant in explaining and predicting their dividend decision within the period under review. The result provides strong support for the explanatory or predictive power of Lintner's model and confirmed that share market price is a representation of market valuation of dividend. Musa (2009) examined whether current earnings, previous dividend, cash flow, investment and net current assets have significant aggregate as well as separate impact on the dividend policy of a cross-section of 53 firms quoted on the Nigerian Stock Exchange (NSE) during the period 1993 to 2002.

He used the five-variable parsimonious dividend policy model developed by Musa (2005). The study concluded that earnings, previous dividend and cash flow all have significant positive impact on the dividend policy of the quoted firms in Nigeria.

3.0 METHODOLOGY

This study falls under the *ex-post facto* design type as it is designed to test an event that has already taken place. Therefore, it deals with historical facts about dividend policy and its effects on stock prices of Nigerian firms.

Secondary data of the sample firms were obtained from their annual reports, FACTBOOK and Stock Exchange Daily Official List (SEDOL). Both are published by the Nigerian Stock Exchange (NSE). The period of the study from 1996 to 2015. The research sample in this study is determined on the availability of data for the quoted firms in Nigeria. Using purposive sampling technique, the study will adopt three firms as case study namely:

Nestle Nigeria Plc,
Unilever Nigeria Plc and
Guinness Nigeria Plc

The data used for this study are valid and reliable as they are obtained from annual reports of selected companies which have been subjected to independent audit by an external auditor and prepared in accordance with the requirements of the Nigerian Stock Exchange. Data for this study are analyzed using ordinary least square (OLS) technique to evaluate the relationship between the two variables i.e dependent and independent variables.

The ordinary least square (OLS) models:

$Y = Q + {}_{x} + \mu$

Where:

Y = Dependent variable
Q = Intercept parameter
= Slope of the regression
x = Independent variable
μ = Random or stochastic term (error term)

The functional relation of the model for this study is given as:

SP = f (DY + RE + EPS)

$SP = Q_0 + {}_1DY + {}_2RE + {}_3EPS + \mu$

Where:

SP = Stock price
DY = Dividend yield
RE = Retained Earnings
EPS = Earnings Per Share

4.0 ANALYSIS AND FINDINGS

Ordinary Least Square (OLS) technique of regression was used to determine the effect of dividend policy on stock prices of selected public companies in Nigeria form 1996 to 2005 using Statistical Package for Social Sciences (SPSS) version 20. The results are as presented below:

Data Analysis and Interpretation

Data Analysis of Nestle Nigeria Plc Results

Statistic	Hypothesis one	Hypothesis two	Hypothesis three
R	0.853	0.974	0.996
R^2	0.728	0.949	0.991
AR^2	0.713	0.946	0.991
Error estimate	9.165	3.969	1.622
Sum of square	4044.642	5273.022	5509.207
Residual sum of squares	1511.908	283.528	47.343
DW	1.353	1.784	1.886
C	-1.124	-9194	2.427
Ceoff.	2.206 E-606	1.861	1.189 E-006
P-value	0.000	0.000	0.000

From the result above, dividend yield has positive and significant impact on stock prices of Nestle Nigeria Plc. This can be seen with the significance value (P-value) of 0.000 < 0.05, hence, the model is significant. Earnings per share has positive and significant impact on stock price of Nestle Nigeria Plc with the significance value (P-value) of 0.000 < 0.05. This means that the model is significant. It can also be seen that retained earnings has positive and significant impact on stock prices of Nestle Nigeria Plc with significance value (P-value) of 0.000 < 0.05 indicating that the model is significant.

From the table above, the Durbin-Watson statistics is 1.353 and since it is less than 2, this indicates there is a positive serial correlation. The constant or intercept is -1.124. This infers that when all the model parameters are zero, there will still be an effect of -1.124 on the stock price. This is accounted for by other factors not specified in the model. Based on the above information, the estimated regression model is represented as follows:

SP = 1.124+2.206E-006DY + μ

Data Analysis of Guinness Nigeria Plc results

Statistic	Hypothesis one	Hypothesis two	Hypothesis three
R	0.093	0.118	0.355
R^2	0.009	0.041	0.126
AR^2	-0.046	-0.041	0.077
Error estimate	3441.612	3432.577	3232.105
Sum of square	1874450.225	68019.669	27041865.577
Residual sum of squares	213204420.725	2992283.228	188037005.373
DW	0.923	0.900	0.938
C	4395.829	5102.9	5118.858
Ceoff.	-0.913	-1.708	-7.553E-005
P-value	0.695	0.620	0.125

From the result above, dividend yield does not have positive and significant impact on stock prices of Guinness Nigeria Plc. This is evidenced with significance value (P-value) of 0.695 > 0.05. Also, earnings per share does not have positive and significant impact on stock prices of Guinness Nigeria Plc with the significance value (P-value) of 0.620 > 0.05. Retained earnings does not have positive and significant impact on stock prices of Guinness Nigeria Plc from the significant value (P-value) of 0.125 > 0.05.

The value of Durbin-Watson statistics 0.923 from the analysis above is less than 2.00. This indicates that the model shows positive serial correlation. The constant or intercept is 4395.829. This implies that when all the model parameters are zero, there will still be an effect of 4395.829 on the stock price. This is accounted for by other factors not specified in the model. Based on the information above, regression model is represented model is represented as follows:

SP = 4395.829-0.913DY + μ

Data Analysis of Unilever Nigeria Plc Results

Statistic	Hypothesis one	Hypothesis two	Hypothesis three
R	0.269	0.572	0.623
R^2	0.072	0.328	0.388
AR^2	0.021	0.290	0.354
Error estimate	0.725	0.617	0.589
Sum of square	0.739	3.343	3.957
Residual sum of squares	9.461	6.857	6.243
DW	1.219	1.354	1.725
C	1.462	1.143	0.922
Ceoff.	1.610E-007	0.857	1.931E-007
P-value	0.251	0.008	0.003

From the result above, dividend yield does not have positive and significant impact on stock prices of Unilever Nigeria Plc. This is based on the empirical finding with the significance value (P-value) of 0.251 > 0.05. However, earnings per share has positive and significant impact on stock prices of Unilever Nigeria Plc with P-value of 0.008 < 0.05. Retained earnings also followed the pattern of earnings per share as it also has positive and significant impact on stock prices of Unilever Nigeria Plc with the significance value (P-value) of 0.003 < 0.05.

Durbin-Watson statistics show 2.031 and since it is above 2, this indicates that there is a negative serial correlation. The

constant or intercept of 0.638 implies that when all the model parameters are zero, there will still be effect of 0.638 on stock price. This is accounted for by other factors not specified in the model. Based on the above information, the estimated regression model is represented as follows:

SP = 0.638 + 5.393E-008DY + 0.656RE + 1.379E-007EPS +μ

The significance value (P-value) of 0.004 is less than 0.05, the model is significant. Therefore, we conclude that there is positive and significant relationship between stock prices and dividend yield, retained earnings and earnings per share of Unilever Nigeria Plc.

Data Analysis of General Model: SP = ? $_0$ + β_1DY + β_2RE + β_3EPS + μ

Statistic	Nestle Nigeria Plc	Guinness Nigeria Plc	Unilever Nigeria Plc
R	0.997	0.358	0.743
R^2	0.995	0.128	0.552
AR^2	0.994	-0.035	0.468
Error estimate	1.343	3423.117	0.534
Sum of square	5527.703	27595199.840	5.631
Residual sum of squares	28.847	187483671.110	4.569
DW	1.795	0.931	2.031
C	1.442	4994.846	0.638
Ceoff.			
Dividend yield	-2.855E-007	0.602	5.393E-008
Earnings per share	.283	-0.195	0.656
Retained Earnings	1.133E-006	-7.957E-005	1.379E-007
P-value	0.000	0.520	0.004

5.0 CONCLUSION AND RECOMMENDATIONS

The study was embarked on in order to determine how dividend policy impacts on market price of selected Nigerian manufacturing firms. Data were obtain for twenty years i.e from 1996 to 2015 of three manufacturing firms. Results showed that dividend pattern or dividend paid by Nigerian firms depends on earnings per share, except for few ones that paid relatively constant dividends even when their earnings per share is nothing to write home. This align with the Lintner's (1956) findings that decrease in or non-payment of dividend could covey a wrong signals to investors.

The study therefore recommends as follows:

1. Management of Nigerian firm, in formulating dividend policy, should have optimal policy that satisfies its shareholders.
2. Firms in Nigeria should endeavour to practice regular dividend policy so that investors could know in advance whether or not a firm dividend policy will tally with their expectations.
3. Quoted firms in Nigeria to formulate dividend policy that will maximize shareholders wealth.
4. Nigeria firm should adopt trade-off policy between dividend payment and retained earnings that would increase the shareholders wealth in terms of cash and/or stock dividend as well as capital appreciation.
5. Managers should act in the best interest of investors in order to reduce the agency problem.
6. Government should embark on enlightenment campaign to increase the level of awareness of the public so that more people invest their surplus funds for the growth of the economy.
7. Government should device a system that will help reduce incidence of unclaimed dividend in Nigeria.

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