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Dividend Payout Study of Companies in Bangladesh: A Preliminary Study

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ABSTRACT

Dividend announcement is considered as a signal to convey information to the market. Many researchers have found relevance of signalling power of dividends to market. Still there are arguments among researchers whether dividend announcements really convey any information or not. From the literature review it is found that dividend announcements are best in conveying information in the absence of perfect capital market, rational behaviour and taxes. Dividend initiations and omissions have significant impact on firms' earnings, shareholders' wealth and give signal about the current and future management policy of a firm.

Keywords: Dividends, Earning, Industry Category, Payout Timings, Taxation.

INTRODUCTION

Dividend Payout Announcement Policy is considered as a signal to convey information to the market. Many researchers have found relevance of signalling power of dividends to market. Still there are arguments among researchers whether dividend announcements really convey any information or not. [Charest, G. 1978] A dividend is a payment made by a corporation to its shareholders, usually as a distribution of profits. When a corporation earns a profit or surplus, it can either re-invest it in the business (called retained earnings), or it can distribute it to shareholders. A corporation may retain a portion of its earnings and pay the remainder as a dividend. Distribution to shareholders can be in cash (usually a deposit into a bank account) or, if the corporation has a dividend reinvestment

plan, the amount can be paid by the issue of further shares or share repurchase. In this study we want to show about the company's perceived earning, industry category, Taxation, payout timing, shareholders wealth and how affect the company's dividend. It was found that Dividend paying intension is associated with the company's Industry Category for buying a share. The research shows that the after tax profit of a company, distributed to its shareholder according to the number and class of share held by them is dividend. Earnings have a significant effect on dividend. [Miller, M. and Rock, K. 1985] If the earnings of a company increased the dividend will be increased, price may affect the earnings most significantly on it. If the level of the Tax rate increases, the dividend reinvestment will decrease and the large company has the ability to pay the shareholder's dividend. [Lintner, J. 1956] Timing of the announcement also has a significant effect on dividend because early dividend announcement and delayed announcement brings good and bad news for the shareholder's. Different companies has their own payout policy to whenever announcement their dividend payout. So the payout timing has the significant impact of payout policy. [Smith, C., W. And Warner, J., B. 1979]. The shareholder's wealth effect the dividend of the company due to fall of share price and the additional tax value and other cost. So we tried to analyse the relationship between these variables, their reliability and validity by conducting different multi testing analysis and assessing the percentage rate in order to determine how these variables have an effect on the Dividend Payment intension for a company.

STATEMENT OF THE PROBLEM

Dividend Payout Announcement Policy is formulated by the board of directors of a company in order to make decision how much earnings would be distributed among the shareholders as their reward for making investment in the given company in the form of dividend and how much would be retained within the company as a retained earnings. Dividend policy is an important area of research in corporate finance. [Ghosh, C. and Woolridge, J.,R. 1988] Even though a number of researches have been conducted on dividend policy, a limited number of studies have revealed the applicability of the dividend theory on some listed companies in an organized stock exchange. Dividend policy is a major financing decision that involves with the payment to shareholders in return of their investments. Every firm operating in a given industry follows some method of dividend payment pattern or dividend policy and this provides as a financial indicator of the firm [Aharony, J. and Swary, I. 1980] Thus, demand of the firm's

share should to some extent, dependant on the firm's dividend payment pattern. There are those who suggest that dividend policy is irrelevant because they argue a firm's value should be determine by the basic earning power and business risk of the firm,[De Angelo, H. et al. 1996] in which case value depends only on the income (cash) produced, not on how the income is split between dividends and retained earnings and opponents of this statement called dividend is irrelevant, that investors care only about the total returns they receive, not whether they receive those returns in the form of dividends, [Elton, E., and Gruber,M . 1970] capital gains or both. Dividend policies are categorized mainly in cash and stock dividend. In Bangladesh the private commercial banks are known to follow stock dividend mostly for the recent implementation of Basel-II frame work. Therefore requiring banks to comply with MCR where they are encouraged to distribute stock dividend rather than cash dividends. There are four dividend dates that are important to shareholders: declaration date, record date, ex-dividend date, and payment date. Research has been done that show evidence that stocks show relatively high average excess returns on the payment dates of dividend [Balachandran,B. and Nguyen, T., A. 2004]. In Bangladesh, there is a general tendency among investors to hold onto their shares till the record date so that they get entitled for dividend, and then sell it off after the record date. This results in an increase in share supply which might result in price decrease. [Fan, J.,P.,H. and Wong, T.,J. 2002]. While as, in the global market, the firms and stockholders follow the traditional dividend theories. Investors' revisions to forecasts of future cash flows and discount rates are a central issue in understanding stock price movements. At present, the empirical evidence points to the conclusion that prices are driven mainly by revisions to discount rates and those cash flows are largely unpredictable. As expressed by [Brickley, J. 1983] in his paper it was seen that when discussing the development of the literature over the last 40 years: "Most views of the world changed 100%: we thought 100% of the variation in the market dividend yields was due to variation in expected cash flows; now we know 100% is due to variation in discount rates." That most of the empirical evidence points to the fact that dividend growth appears unpredictable and that all the movement in the DP ratio is driven by news about future discount rates is a remarkable and troubling finding. So, it is difficult to compare Bangladesh's dividend policies to that of the Global market policies. Payouts, yields are affected by different variables in either segment. Miller and Modigliani [Miller,M.,H. and Modigliani, F. 1961] put forward that matching takes place between investor clienteles who demand dividends and those firms that feel paying them is less costly, that is, companies set their payout policies and investors sort them based on their preference for dividends. On the other hand,

firms may respond to the preferences of their current shareholders. [Bulan et al. 2007]. According to authors, the return predictability regressions have small predictive power and are sensitive to the choice of forecasting instruments, backed-out cash flow news or future discounts inherits any potentially large misspecification error in the estimation of discount rate news. [Baker, H., K. and Powell, G., E. 1999] A share of the after tax profit of a company, distributed to its shareholder according to the number and class of share held by them is dividend. Earning has a significant effect no dividend. If the earning of a company increase the dividend will be increase, price may affect the earning mostly significant on it. [Bernheim, D. 1991] If the level of the tax rate increases, the dividend reinvestment will decrease and the large company has the ability to pay the shareholder's dividend. Timing of the announcement also has a significant effect on dividend because early dividend announcement and delayed announcement brings good and bad news for the shareholder's.[Cheng et al. 2009] Different companies has their own payout policy to whenever announcement their dividend payout. So the payout timing has the significant impact of payout policy. The shareholder's wealth effect the dividend of the company due to fall of share price and the additional tax value and other cost.[Fan, J.,P.,H. and Wong, T.,J. 2002].

The problem statement of the research is **"to identify company's perception about the dividend payout policy and shareholder's viewpoint on companies industry category, timing and policy, earning, and taxation towards dividend payout and linking all these variables together and finding out shareholder's share buying intension and companies dividend payment intensions."**

PURPOSE OF THE STUDY

The purpose of this study is to know about the company's perceived earning, industry category, Taxation, payout timing, shareholders wealth and how affect the company's dividend. Company's Dividend research can be an effective tool that a company can use to experience regarding dividend structure. [John, K. and Williams, J. 1985], [Bhattacharya, S. 1979], [Miller,M.,H. and Modigliani, F. 1961]

- The level of dividend reinvestment will be reduced for high tax rate.
- For the high tax rate the large company capable enough to pay dividend but the small company discourages to pay dividend.
- If the company give announcement at early than it brings good news for the shareholder.

- If dividend announcement are delayed it means that management have decided to reduce the dividend.
- Relationship between dividend announcement and earning are significant because the earnings increase or decrease at least a year before dividend initiation or omission announcement. [Asquith, P. and Mullins, D.,W., Jr. 1983][Balachandran, B. 2003]
- The stock price reaction due to dividend initiations or omission is closely related with changes in earnings in the year before and after dividend declaration.
- The present value of additional tax and present value of other cost will decrease shareholders wealth.[Benartzi, S. et al. 1997]
- Reduction in dividend may cause the price of share to fall and can have negative impact on shareholders wealth.[Asquith, P. and Mullins, D.,W., Jr. 1983]
- Industry category in not only specific to size but to type of business as well. This is because some business may have higher profit margin in spite of small size and hence pay higher dividend.
- Generally it is seen that bigger industries pay large dividend.

HYPOTHESIS

- ***H1-*** Dividend paying intension is associated with the company's industry category for buying a share.
- ***H2-*** Payout timing announcement will affect shareholder's intension to buy a share.
- ***H3-*** Higher tax rate has impact on dividend initiation policy
- ***H4-*** Dividend payment is associated with re-investment and has a positive impact on shareholders wealth.

SAMPLE UNIT

The sample unit of research design is totally dependent on different company's behaviour that pay dividend to the shareholders. According to the collection of information/data the participants face the questionnaires prepared by the researchers. The data which are gathered by the researcher are the secondary data which are collected from the company's annual report, share prices, financial statements, etc. which are publicly available. The population for this study consisted of the companies which are listed in the Dhaka Stock Exchange (DSE). For the study purpose, the sample consisted of the shareholder's, investors and the companies normal shareholders.

SAMPLE

Sample size defines how many people are selected for the study. We selected investors and the shareholders of different ages, different educational backgrounds, occupation and the income level. We chose twenty investors and a company for our study. This study utilized probability sampling technique that involved selecting participants randomly for surveying. When we chose our sample we gave priority to some investors who are well known by us and selected ten different companies where we observed and studied the financial statements, annual reports of those companies.

INSTRUMENT

The questions used for data collection are all close ended questions. Liker scale is used for respondents to response. There are 18 questions in total for

measuring all the variables. Each variable is measured by at least 3 questions. In our survey we followed a 5 point "Likert Scale" which consisted of the following criteria's: Strongly Agree, Agree, Neither Agree or Disagree, Disagree, Strongly Disagree.

DATA COLLECTION

Data collection procedure for this particular research was entirely primary data collection. A questionnaire was used to survey the investors in order to obtain qualitative data. The survey was carried out at different firms and companies across Dhaka city. It encompasses 20 respondents from different firms and companies. Potential respondents were approached and asked if they would like to participate. Those that agreed were given the questionnaire. We conducted our survey in one week.

DESCRIPTIVE ANALYSIS

- For our survey there were 15 male respondents which represent 90% of total sample size and 5 female which consisted 10%. Most of our participants were between 36-40 years of age that represents 35% of total sample. We had 2 participants who were 20-25 that was 10%. We had also 4 participants between 26-30 years and 41-above years and the percentage represents 20% and 20% of total sample.
- In our survey most of the participants are businessman and their percentage was 35%, then 30% are private service holder,, 15% are Govt. service holder and rest of students and Retired persons.
- We have 5 categories of income and 8 participants are in tk 30,001-50,000 income range which is 40% of total sample. 6 participants are in tk 20,000-30,000 income range which is 30% of total sample. Then 2 participants are in tk 50,001-70,000 income range which is 10% and rest of 5%.

FREQUENCY TESTING

- For the Q.1 "increase or decrease of earnings influences the stock investment" - 40% from the total respondent Strongly Agree, 20% Agree, 20% Neither Agree nor Disagree, 10% Disagree and 10% Strongly Disagree with this statement.

- For Q.2 "relationship between dividend announcement and earning" - 55% from the total respondent Agree, 15% Strongly Agree, 10% Neither Agree nor Disagree, 5% Disagree and 10 % Strongly Disagree with the question.
- For Q.3 "the market reaction to earning of the company" - 25% from the total respondent Agree, 35% Strongly Agree, 10% Neither Agree nor Disagree, 25% Disagree and 5% Strongly Disagree with the question.
- For Q.4 "the intension of paying dividend of bigger industry" - 50% from the total respondent Strongly Agree, 20% Agree, 10% Neither Agree nor Disagree, 10% Disagree and 10% Strongly Disagree with this question.
- For Q.5 "influencement of investment for industry category" - 35% from the total respondent Strongly Agree, 25% Agree, 5% Neither Agree nor Disagree, 25% Disagree and 10% Strongly Disagree with this question.
- For Q.6 "inability to pay dividend of smaller industry for their losses" - 25% from the total respondent Strongly Agree, 15% Agree, 20% Neither Agree nor Disagree, 25% Disagree and 15% Strongly Disagree with this question.
- For Q.7 "influence of higher taxation rate to the firm's initiation policy" - 45% from the total respondent Strongly Agree, 25% Agree, 15% Neither Agree nor Disagree, 10% Disagree and 5% Strongly Disagree with this question.
- For Q.8 "effect of higher taxation rate over the dividend reinvestment" - 30% from the total respondent Strongly Agree, 35% Agree, 10% Neither Agree nor Disagree, 15% Disagree and 10% Strongly Disagree with this question.
- For Q.9 "effects of taxation on cash dividend and stock investment" - 20% from the total respondent Strongly Agree, 30% Agree, 10% Neither Agree nor Disagree, 30% Disagree and 10% Strongly Disagree with this question.
- For Q.10 "prediction of dividend announcement depend on previous announcement"- 30% from the total respondent Strongly Agree, 40% Agree, 10% Neither Agree nor Disagree, 10% Disagree and 10% Strongly Disagree with this question.
- For Q.11 "effects of early announcement on for the shareholder" - 45% from the total respondent Strongly Agree, 20% Agree, 15% Neither Agree nor Disagree, 10% Disagree and 10% Strongly Disagree with this question.
- For Q.12 "effects of postponement of dividend announcement" - 30% from the total respondent Strongly Agree, 40% Agree, 15% Neither Agree nor Disagree, 10% Disagree and 5% Strongly Disagree with this question.

- For Q.13 "expectation of higher shareholder wealth" - 45% from the total respondent Strongly Agree, 25% Agree, 5% Neither Agree nor Disagree, 15% Disagree and 10% Strongly Disagree with this question.
- For Q.14 "effects on shareholder wealth due to the reduction of dividend payout" - 30% from the total respondent Strongly Agree, 30% Agree, 15% Neither Agree nor Disagree, 15% Disagree and 10% Strongly Disagree with this question.
- For Q.15 "effects of shareholder wealth for additional tax and other cost" - 25% from the total respondent Strongly Agree, 30% Agree, 20% Neither Agree nor Disagree, 15% Disagree and 10% Strongly Disagree with this question.
- For Q.16 "influencement of regular dividend payout to the investor" - 50% from the total respondent Strongly Agree, 25% Agree, 10% Neither Agree nor Disagree, 10% Disagree and 5% Strongly Disagree with this question.
- For Q.17 "information about the future cash flow" - 35% from the total respondent Strongly Agree, 15% Agree, 20% Neither Agree nor Disagree, 20% Disagree and 10% Strongly Disagree with this question.
- For Q.18 "information on current earning of a firm" - 40% from the total respondent Strongly Agree, 25% Agree, 15% Neither Agree nor Disagree, 10% Disagree and 10% Strongly Disagree with this question.

CORRELATION

Pearson correlation is used to see the strength of relationship between variables. In significance on $p_{\leq}$ 0, then null hypothesis will be rejected and alternate will be considered. In our testing we find the value of Earnings (IV) and Dividend (DV) which is 0.228which is weak. Taxation and Dividend (DV) has a value of0.0929 which means there is a strong relationship between these 2 variables. The Industry Category (IV) and Dividend (DV) has the value of 0.179 which very weak and there is a very weak relationship between them. The value of Payout Timing (IV) and Dividend (DV) is 0.483; there is a moderate relationship between these 2 variables. The value of Shareholders Wealth and Dividend is 0.280 which indicates a weak relationship. The Spearman rank-order correlation coefficient (Spearman's correlation, for short), is a non-parametric measure of the strength and direction of association that exists between two variables measured on at least an ordinal scale. It is denoted by Greek letter ρ. The test is used for either ordinal variables or for interval data that has failed the

assumptions necessary for conducting the Pearson's product-moment correlation. For our research if the correlation coefficient $\rho \neq 0$ and significance $\alpha < 0.05$ then the alternative hypothesis is acceptable which means there is a relationship between the two variables. In the relationship between Earnings and Dividend, $\rho = 0.406$ which is $\neq 0$ and $\alpha = 0.076$ which is greater than 0.05. This means there is a rather poor relationship between Earnings and Dividend. So we are not accepting it. Relationship between Industry Category and Dividend, $\rho = 0.273$ which is $\neq 0$ and $\alpha = 0.224$ which is greater the 0.05. This means there is a poor relationship between Industry category and Dividend. So we are not accepting it. In the relationship between Taxation and Dividend, $\rho = 0.115$ which is $\neq 0$ and $\alpha = 0.564$ which is greater than 0.05. This means there is no relationship between Taxation and Dividend. So we do not accept it. In the relationship between Shareholders Wealth and Dividend, $\rho = -0.112$ which is < 0 and $\alpha = 0.639$ which is greater than 0.05. This means there is no relationship between Shareholders Wealth and Dividend. So we do not accept it.

REGRESSION ANALYSIS

R square values represent how much a dependent variable is explained by the independent variable and if $P < 0$ then null hypothesis will be rejected and alternate will be considered. About 8% of earnings variability effects dividend payment ratio. Around 13.40% Industry category variability effects dividend payment ratio. 22.90% Taxation effects dividend payment ratio. 25.60% Payout Timing effects the dividend payment ratio and around 25.80% Shareholders Wealth effects dividend payment ratio.

COEFFICIENT

In Coefficient, significant level, if we take earning is only variable for the dividend payment structured the value is .228 which is accepted. If we take earning with Industry category the value is .415 and .318 which is also accepted. If we take earning, Industry category, payout timing, tax and shareholder wealth the value are .281, .178, .289, .475, .834 which all are accepted.

CONCLUSION

Information content of dividend announcement is considered as one of the most controversial topics in finance literature. Finance researchers have engaged in extensive research to explain what kind of information a dividend announcement contains. As we found from the literature, many researchers claimed that dividend information signals a lot of information to the market. Researchers claimed dividend announcements give information about earnings, current and future financial condition of a firm and future management policy. Other group of researchers claim that dividend announcements do not provide any proper information to the market. Although dividend policy is used to convey information the market, but dividend may not work as a perfect signal unless markets understand the information and act timely and accordingly. Insider trading activities will also bring inequity in the market. The larger shareholders and directors will exploit the advantage of dividend decision prior to the market and the minor shareholders will be the ultimate the victim of such inside trading. Information content of dividend announcement is well documented in the literature of finance. Researchers have developed many different models for explaining dividend Information contents of dividend announcements. Yet researchers have different views. Future research needs to extensively build a concrete theory on the information content of dividend announcements. By listing and analysing the gaps in the existing research it is fair to say that there is still scope to further understand the dynamics of dividend announcements.

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