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TO STUDY THE IMPACT OF DIVIDEND POLICY ON SHAREHOLDER VALUE

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1 INTRODUCTION

The dividend policy of a company is its conscious dividend policy in determining the percentage of shareholder returns in dividends and the percentage of shareholder funds in retained earnings for investing in the future. It plays a significant role in business financial decisions, affecting the business's capital structure, investment structure, liquidity management, and the long-term valuation of the business.

A good dividend policy achieves a balance between two critical corporate goals: maximizing the value of the shares outstanding to the market and providing adequate funds internally to continue the business. Reinvesting profits, on the other hand, enhances a company's ability to fund future projects, expand its business, and maintain financial agility while minimizing reliance on external funding sources. On the other hand, dividend payments are regular, consistent, budget-friendly, and improve investor confidence and reflect shareholders' actual earnings.

Typically, the dividend policy is established based on the financial condition, growth stage, earnings regularity, and investment opportunities of the business. An example of this is the stable dividend policies of more established companies that are also financially stable and have steady growth. Because a residual dividend policy relies on the money left over after all potential investments have been made, distributions are more erratic and dependent on investments. An irregular dividend policy, however, is a more flexible policy that entails dividend payments changing from period to period based on cash flow, earnings performance, or financial strategy (Ross et al., 2019).

Dividend policy is part of the financial planning process and also has a significant signaling effect on the capital markets. Regular and reliable dividend payments can signal that the company is likely to be financially secure, efficient in its operations, and generate future income, thus attracting more investors to the stock and boosting its market value. (Brigham & Ehrhardt, 2022) On the other hand, unforeseen shifts in dividend payments—especially a decline—can indicate financial problems or decreased profitability, which frequently results in unfavorable market reactions and more share price volatility.

The dividend policy is not a simple choice of the dividend payment; it is a business policy that, over time, can be beneficial for the company, can have an impact on investor expectations, can be a sign of management's confidence, and can convey the company's financial performance and governance.

1.2 Concept of Dividends

As a return on their investment, shareholders get dividends, which are a fraction of a company's profits. They can get paid in cash, stock, or other assets depending on the company's finances. The prosperity and stability of the company's finances are reflected in dividends.

1.2.1 Importance of Dividend Policy

The dividend policy has a great impact on the market value of the company's shares and the expectations of the investors. One of its key reasons is that investors often seek a consistent and predictable dividend income, especially during low-risk investment times.

A consistent dividend policy increases investor confidence and demonstrates the company's good cash flow control and stable profit. This could lead to a rise in the company's demand and, in turn, its market value (Ross et al., 2019).

Also, dividend policy assists the management in determining the amount of profit to be reinvested in the business. Internal financing comes largely from retained earnings, and a properly designed dividend policy will not result in the sacrifice of growth opportunities, yet provide the investor with a reward. (Brigham & Ehrhardt, 2022).

1.2.3 Dividend Policy Importance

The three primary objectives of dividend policy: The primary goal of dividend policy is the creation of sustainable growth for the company while maximizing shareholder value. The balance between sharing gains and retaining sufficient cash for future investments is a challenge for businesses.

Stable payouts to keep investors calm, enough cash to meet operational needs, and support long-term growth targets are key objectives. Establishing a steady dividend pattern that represents financial stability and lessens variations in shareholder returns is another crucial goal (Pandey, 2021).

Another important factor of dividend policy that can be achieved by the effective use of retained earnings rather than borrowing funds from outside the company is to cut down the cost of financing and enhance the overall efficiency of the capital structure.

1.3 Types of Dividends

There are a number of categories of dividends based on the distribution method and the financial position of the company. Every kind has a distinct function and is employed in certain financial circumstances. There are various categories of dividends, the most common being cash dividends, property dividends, stock dividends, liquidation dividends, intermediate dividends, and final dividends (Brigham & Ehrhardt, 2022).

- **Cash Dividend:** The most typical kind of dividend, in which shareholders get paid directly, is a cash dividend. It is frequently spread through banking systems and paid per share. Cash dividends are preferred by investors who require regular income. They do, however, also lower the company's cash reserves, which might have an impact on liquidity if improperly handled. The more consistent the revenue and cash flows of a business, the more likely it is to pay a regular cash dividend (Gitman et al., 2018).

- **Stock Dividend:** A dividend in which the owners receive additional shares instead of cash payments. The number of outstanding shares increases, but has no immediate effect on the company's cash flow. Stock dividends are often used by businesses to pay a dividend to shareholders and retain money for future expansion. Stock dividends can lead to long-term capital gains without any change in the total value of the investment (Ross et al., 2019).

- **Property Dividend:** A distribution of non-cash assets to shareholders (such as investments, securities, or tangible assets). Occasionally, this type of dividend is given when the business has insufficient liquid capital. There is a need for asset appraisal for property dividends, and regulatory concerns may arise. Typically, they are used in special situations such as asset liquidation or restructuring (Pandey, 2021).

- **Liquidating Dividend:** When a business is shutting down entirely or partially, it pays out a liquidation dividend. It's a repayment of capital, not a payout of profits, as with standard dividends. Dividends of this sort are usually paid when the company is winding up, or it sells substantial assets. It is a large-scale restructuring or the end of the business's continued operating life (Brigham & Ehrhardt, 2022).

- **Interim Dividend:** Prior to the annual accounts being finished, an interim dividend is announced and distributed throughout the fiscal year. Typically distributed at the end of the first half or quarter of the year, when the business is performing well, and on anticipated earnings. Interim Dividends also provide shareholders with rewards early and indicate management's confidence in ongoing profitability. However, in order to prevent overspending, they need rigorous financial forecasts (Gitman et al., 2018).

- **Final Dividend:** A declaration of dividend at the end of the financial year following the preparation of the audited financial statements. Approved at the annual general meeting, typically higher and more formal than interim dividends. Final dividends are the company's final profit distribution for the year and show the company's overall financial performance. They are more reliable since they are based on the financial results that have been verified (Ross et al., 2019).

2 EFFECT OF DIVIDEND PAYMENTS ON THE VALUE OF COMPANY/TO SHAREHOLDERS

2.1 MARKET CAPITALIZATION

Market capitalization is the total value of a company. It's measured by the stock price times the number of shares issued. For example, a company that has 1 million shares that are selling for $10 each would have a market capitalization of $10 million. This means you could buy that company for $10 million if you had the money and all the current stockholders were willing to sell you their shares.

Market capitalization is usually called market cap for short. It also refers to the total value of a stock exchange.

2.2 SHAREHOLDERS' VALUE CREATION AND ITS LINKAGE WITH DIVIDEND POLICY DECISIONS

Several research studies have recognized that a dividend policy can have an effect on the future value of the business if it is developed and carefully implemented. The purpose of optimizing wealth is a generally agreed goal of the group, as it reconciles the complex, frequently conflicting stakeholder interest. As a consequence of many recent developments, the interest in shareholder value is gaining momentum:

- The possibility of corporate takeovers by those searching for under-valued assets
- Remarkable support from business leaders who took the approach
- A growing awareness that the valuation of the company's shares does not consistently link to conventional accounting measures like EPS and ROI
- Reporting of returns to shareholders and other indicators of business press success.
- A growing understanding that managers' long-term compensation must be closely related to shareholders' returns.

The Shareholders Value method calculates the economic value of an investment by discounting expected cash flows by the cost of capital (e.g. company's shares, plans, mergers and acquisitions). These cash flows serve as a basis for shareholder dividend returns and the rise in share price. An ongoing concern must strive to increase its capacity to generate cash. The ability of a corporation to allocate cash to its different constituencies depends on the ability to raise capital from its activities and on the ability to receive additional funds from external sources. Two basic external sources are debt and equity funding. The credit power and market value of the shares depend on the capacity of a company to produce cash. The market value of the securities impacts directly on the second source of funding, namely equity financing.

The higher the share price for a certain amount of funds needed, the lower dilution would be borne by existing shareholders. The financial ability of management to deal successfully with corporate claimants therefore often stems from a rise in the valuation of shares. This rise in share value can be accomplished by rewarding shareholders with dividend returns and capital gains. The most famous statement about the relationship between the policy on dividends and corporate value stated that due to the investment policy of the company, the payout policy it opts to follow will not affect the present price or total return of its shareholders in the presence of perfect markets."

However, "market imperfections as differential rates of taxation, information asymmetries between insiders and outsiders, conflicts of interest between managers and shareholders, cost of transaction, cost of flotation and the irrational behavior of an investor may make the dividend decision of relevance"

Another market imperfection is information asymmetries, as opposed to information asymmetries between insiders (for example, managers) and outside parties (for example investors). Agency disputes, deriving from different priorities of company stakeholders, are the third market imperfections.

3. OBJECTIVES

The Company's value depends upon the value of its shares in the markets and the pace of increase in same. There are various other factors that impacts the value of the Company. Earlier few researches have been carried out on same and this research is carried out with the following objectives. The objectives of the study are as follows:

- To study the dividend policy determinants
- To study the impact of dividend policy determinants on market capitalization.
- To study the dividend distribution on value creation for shareholders.
- To study the dividend behavior pattern for companies under research.

4.1 HYPOTHESIS

H_0: There exists a positive relationship between dividend policy determinants and valuation of companies.

H1: There is no positive relationship between the dividend policy determinants and valuation of companies

H0:- There is a significant impact of dividend policy determinants on market capitalization.

H1:- There is no significant impact of dividend policy determinants on market capitalization.

H0: There is significant impact of dividend distribution on value creation for shareholders

H1:- There is no significant impact of dividend distribution on value creation for shareholders.

4.2 THE DATA AND SAMPLE

The study is focused on three sectors IT, FMCG and Service sector (Banking Sector).

5. UNIVERSE & SAMPLE SIZE.

The data analysis shall be undertaken from secondary sources. The whole project will be based on the secondary data based on the detail. The considered companies would be 30 of BSE

The data has been analyzed and available from the balance sheets and other financial statements made available in the "**PROWESSIQ**" software. This data is extensively used by market analysts, research scholars, fund managers and other financial market intermediaries to take infirmed decision regarding investments in these companies. The sample size is chosen from constituent companies of BSE sensitive index as on year 2002.

CONSTITUENT COMPANIES OF BSE SENSEX INDEX SINCE 2002.

Bombay stock exchange BSE is Asia's oldest stock exchange. Based in Mumbai, India, BSE was established in 1875 as the native share and stock brokers association. Prior to that brokers and traders would gathered under banyan trees to conduct transaction (source: - "Bombay stock exchange website").

The BSE index represents every segment of industry and constituent of companies represents 65% of the market capitalization of the companies listed of BSE.

6 DATA COLLECTION

6.1 SECONDARY DATA

Secondary data will be collected from the stock exchange and companies registered under company secretary office (CSO). Secondary data is the data that is readily available from other sources and consists of the information of the companies which are already registered under Bombay Stock Exchange.

- The data has been collected from software named as PROWESSIQ.
- Data frequency taken into consideration at the time of analysis is every fortnight
- The study is sectoral study of Indian firms which includes three sectors IT, FMCG & Service sector (Banking sector).

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