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A Study On The Effect Of Dividend Strategy In Bombay Stock Exchange

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Abstract:

Businesses are torn between using their gains for future investments or allocating a large, little, or none at all as dividends to their shareholders. Companies' dividend policies can either positively or negatively affect the price of their stock since they have to strike a balance between the conflicting interests of various shareholders. The effect of dividend policy on stock prices is investigated in this study. The goal of the study is to ascertain whether stock prices and dividend policies are related in any way. Dividend payment percentages for each of the 100 index businesses were determined by the study. Companies that fall within the dividend payout percentage range of 0%–10% are classified as no dividend yield stocks, 11%–20% as low dividend yield stocks, and 21% and above as high dividend yielding stocks, according to the derived values. Thus, during the period from 2008 to 2020, 16 businesses listed under the Bombay Stock Exchange SENSEX 100 index are chosen as the real sample, with 8 of them being classified as High dividend yield stocks, 4 as Low dividend yield stocks, and the remaining 4 as No dividend produce stocks.

Keywords: shareholders, dividend, representatives, investment, firm, payout, linearity, fluctuations, volatility, stock value.

The topic of dividend policy is still up for debate in academia because financial economists continue to cast doubt on its significance. Dividend policy is one of the few areas of corporate finance policy where practitioners and scholars diverge more than others. There are contradictory patterns in dividend payments and business value in the studies on the subject, ranging from Miller & Modigliani (1961) 1 to Gordon & Linter to Fama & French (2001) 2. The scholarly consensus is that dividends, as a signal to investors from companies, actually don't matter all that much for the market. Investment analysts and business representatives both think that a company's dividend policy is crucial in providing information to stakeholders. Based on economic theory, there is a side that claims it is unimportant or doesn't matter. However, practitioners see it as public information reflecting the gravity of the issue inherent in the market's reaction mechanisms to announcements of dividend policy.

When it comes to investing, a company's dividend policy takes precedence over other financial strategies. Knowing if the company will finance its investment project through internal or external sources is equally crucial. A firm's dividend policy decisions are influenced by several aspects, including investor desire, profits, investment possibilities, annual versus goal capital structure, flotation costs, stability, signaling, government regulations, and taxation. Signaling is one of the key elements influencing the market when there is asymmetric information.

Dividend yield and payout ratios have been shown to correlate inversely with common stock volatility through a variety of theoretical methods. The subject of the type of the dividend and its effect on the share price, as well as whether the market is more volatile to high dividend yield shares than regular shares, arises because dividends can be cash dividends, stock dividends, stock splits, and share repurchases. Research on the market's sensitivity to dividend types is required. Examining the relationship between payouts and share price requires controlling other variables that influence a company's dividend policy.

According to Modigliani and Miller's (1961) dividend irrelevance argument, the dividend policy has no discernible effect on share value since alternative funding sources precisely balance out its effects, making them irrelevant. This theory was developed on the assumption of perfect market circumstances, ignoring factors like as taxes, transaction costs, and asymmetric knowledge. As a result, dividend policies have minimal effect on the businesses' market value. The dividend irrelevance hypothesis must be used cautiously, concentrating on the implications of taxation, information content, agency costs, and other pertinent influencing factors, as the capital market is neither perfect nor comprehensive.

According to the Gordon model (1959) of stock valuation, a stock's fair value is equal to its stock dividend per share plus the difference between the discount rate and the dividend growth rate over the long run. The model postulates that the discount rate will never change and that the firm's dividend would increase steadily over time. According to theory, a rise in the dividend rate will also likely result in an increase in the company's stock value.

The outcome shows the rising trend in share price movement following the announcement of the dividend. Their research' most important conclusion is that positive signaling persisted for just one day following the announcements. Following then, shares' positivity begins to decrease. Their research demonstrates that the Indian market's response to news or events, including share buybacks and dividends, typically varies over the course of a day or two. One may argue that the study is relevant to the current investigation.

The most crucial thing to start with when examining dividend and stock price behavior is an objective function that expresses a company's preference for a dividend-retention mix rather than focusing only on dividend yield or payout ratio. Due to the prevalence of joint stock companies and its accompanying characteristics of ownership and control separation, the firm's major incentives have changed, and this has an impact on the goal function.

This change may be defined as a departure from the primary goal of maximizing the rate of return on capital to a variety of goals, including increasing sales and growing the company. These same set of factors that are driving up the firm's market value also align with the managing agency mode of operation that characterizes Indian businesses. Furthermore, the division of ownership and control suggests that the management and stockholders of the company have different goals and preferences.

Using a straightforward specification of stock return as a function of net profit and dividend-retention ratio together with two control variables, such as the firm's size and debt-to-equity ratio, we have attempted to investigate the link between dividends and stock return. Prior to moving further with the final estimation using panel-data modeling, various structural tests were tried. We are able to employ panel-data modeling because of the exclusive testing of several models. We evaluated the suggested model independently for each of the six industries that we classified for the study using various variable combinations. When the industry categories are specified, the findings show statistical significance and linearity. Regression analysis on the total data is still significant. Nonetheless, the dependent variable's connection is pointing in the expected direction. Put another way, there is a positive correlation between the dividend retention ratio and stock returns. Since there is no statistically significant regression in the case of aggregate data, which includes all of the businesses from the industry groups listed above, the null hypothesis that there is no link between the dependent and independent variables cannot be rejected.

The market moves stock values every day. Prices fluctuate as buyers and sellers determine the relative value of each stock. Basically, supply and demand determine how much shares cost. A stock's price increases when there is a greater demand for it than there is for it. In contrast, the price of a stock would begin to decline if more individuals wanted to sell it since there would be more sellers than buyers. With the alternating bull and bear phases of the stock market, volatility in the return on investment is a necessary component.

The return and volatility of the stock market are influenced by these ups and downs, with share values rising in a bull market and falling in a bear one. One indicator of a highly liquid stock market is volatility. The volatility of each asset affects how securities are priced. Increased volatility in the stock market results in significant fluctuations in stock prices, either rising or falling. Investors move their money to less hazardous assets when stock market volatility rises because they perceive this as an increase in the risk associated with investing in equities.

Through a variety of routes, it affects company investment spending and economic growth. Share price fluctuations and the general public's perception of the status of the stock market are influenced by shifts in the local or global political and economic environments. With the rise in FII investment, return and volatility concerns have gained importance among Indian investors, regulators, brokers, policy makers, dealers, and researchers in recent years. Therefore, an attempt has been made in this study to analyze.

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