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Effect of Dividend Policy on Stock Prices: Analysis of Listed Banks in Nigeria

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ABSTRACT

The purpose of this study was to examine the relationship between dividend payout, retained earnings, corporate tax and stock prices with a focus on the Nigerian banking sector. The population of the study comprises of banks that are listed in the Nigerian Stock Exchange. The study samples were selected using purposive sampling method. Data were collected from the Annual report and accounts of the sampled banks for a period of ten years (2006- 2015). The Ordinary Least Square Regression Model was used to estimate the relationship between dividend pay-out, retained earnings, corporate tax and stock prices with the aid of Statistical Package for Social Science (SPSS). Regression Results shows that dividend pay-out has significant positive relationship with stock market prices. The study also revealed that retained earnings have a significant positive relationship with share prices. Corporate tax, has significant negative relationship with the stock prices of the listed commercial banks in Nigeria.

Keywords: Dividend Payout, Retained Earnings, Corporate Tax, Stock price.

1. INTRODUCTION

One of the jobs of a corporation's board of directors is to set dividend policy, which involves the timing and amount of dividends to pay (Akinsulire. 2010; Eric, 2012; Lashgari & Ahmadi 2014). Some say that dividends are important in attracting investors and supporting stock prices, while others claim that earnings are just as important as dividends. Empirical evidence, while not uniform, some suggested that higher dividends raises stock prices, while dividend cuts hurt prices. Other studies show that higher dividend payments make stock prices less volatile (Adediran & Alade 2013; Attah-Botchwey 2014; Sharif, Ali, & Jan, 2015). The accumulated profits of a firm are recorded in the retained earnings account of stockholders' equity, which is the surplus of assets over liabilities. Retained earnings are the only source for dividend payments, whereas internal growth, in the form of new projects, asset purchases, etc., can be financed using retained earnings, new issues of stock, and/or with debt. Cash dividends, if paid,

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are usually declared and distributed quarterly, Stock dividends are occasional distributions of additional stock to shareholders (Younesi, 2012).

Though stock dividends do not result in any actual increase in value for investors at the time of issuance, they have an effect on stock price similar to that of cash dividends. After declaration of a stock dividend, the stock's price often increases. However, because a stock dividend increases the number of shares outstanding while the value of the company remains stable, it dilutes the book value per common share, and the stock price is reduced accordingly (Hashemijoo, Ardekani & Younesi, 2012; Al Masum, 2014).

The goal of corporate entities is to maximise profit for investment made in the company. The stakeholder's pursued the profit maximization of the firm through their investment, and dividend decisions. Investment decisions involve the selection of positive net present value projects. Financing decisions involve the selection of a capital structure that would minimize the cost of capital of the firm while dividend decisions of the firm determine the reward which investors and potential investors of the firm receive from their investment in the firm (Amuche, 2014). It has been observed that the ability of commercial bank to get the high dividend policy within the regulatory capital environment it operates will make it easy to be able to generate the required capitalisation from the Nigerian stock market especially during the recapitalisation (Isa, 2006). In the light of the above, this study examines the impact of listed banks dividend policy with particular emphasis to the resultants effects of corporate tax, retained earnings and dividend payouts on stock prices of listed banks in Nigeria.

Numerous studies by Fodio (2009), Okafor and Mgbame (2011), Adediran and Alade (2013), Amuche (2014), Machael and Benson (2014) and Osegbue, Ifurueze and Ifurueze (2014) on dividend policy in Nigeria show that dividend policy has positive effect on the value of Nigerian firms. However, these works have not taken into consideration of the corporate tax within which the banking industry operates. The corporate tax situation may play a significant role in the determination of the commercial banks dividend policy. For instance, banks with high tax may pay little cash dividend in order to boost their capitalisation and meet capital requirement and vice versa. For this reason, this study is aimed at determining the impact of dividend policy on the stock price of listed banks in Nigeria with particular emphasis to their tax paid.

There are three objectives of this study. The first objective is to investigate whether dividend payout has a significant effect on stock prices of listed banks in Nigeria. The second objective of this study is to examine whether retained earnings has a significant effect on stock prices of listed banks in Nigeria. The final objective is to investigate the significant effect of corporate tax on stock prices of listed banks in Nigeria.

Some studies have been conducted on dividend policy in Nigeria, most of which are well documented in the literature of accounting and finance. These studies include that of Adediran and Alade (2013) Osegbue, Ifurueze and Ifurueze (2014) who used data obtained from listed firms in Nigerian Stock Exchange (NSE) to examine the relationship between dividend policy and share price. From the above literature, the evaluation of the impact of dividend payout, retained earnings, corporate tax on stock prices is considered essential given limited research on this topical issue in Nigeria. This study is therefore; aimed at filling this gap by investigating the relationship between dividend payout, retained earnings, corporate tax and stock prices of listed banks in Nigeria. The study will be restricted to Nigerian listed banks. The time frame to be cover by the study shall be Ten-year period (i.e. 2006 -2015) using their annual report and accounts. This is considered enough to make a meaningful contribution to the empirical research. The listed bank was selected in this study because they have had sufficient experience on the stock market and they have paid dividends and operated within a regulatory capital framework for quite reasonable time. This research would thereby enrich the existing literature as it provides empirical evidence in the context of Nigerian banking industry.

This paper is organised into five sections. Section one, which is the introduction. Section two, which is the next section review related literature and hypothesis development on the subject matter of the study. Section three discusses methodological issue of the paper, model specification and measures of the variables of the study. Section four is the results and discussion. Finally, section five convey the conclusion and recommendation of the paper.

2. LITERATURE REVIEW, THEORETICAL FRAMEWORK AND HYPOTHESES DEVELOPMENT

Dividend policy has been a most debateable subject in the area of finance. Numerous studies on dividend policy has been conducted by many renowned researchers like, Lintner (1956); Miller and Modigliani (1961); Bhattacharya (1979) and more recently, DeAngelo et al. (2006), Al- Malkawi (2007) and Hussainey, et al. (2010).Van Horne (1996) explains that stock dividend should simply be seen as the payment of additional stock to shareholder. Pandey (1999) argued that Dividend policy is a decision by the financial manager whether the firm should distribute or retain all profit or to distribute a portion and retain the balance. Dividend policy is an important aspect of corporate finance and dividends are major cash outlays for many corporations. Suleiman (1999) described dividend as a periodic payment to shareholders to compensate them for the use of their funds by the firm that is making the payment and it comes in different forms. Kurfi (2003) argued that dividend may be paid on common stock; and for reason, it is usually stated as a percentage of the value of the stock,

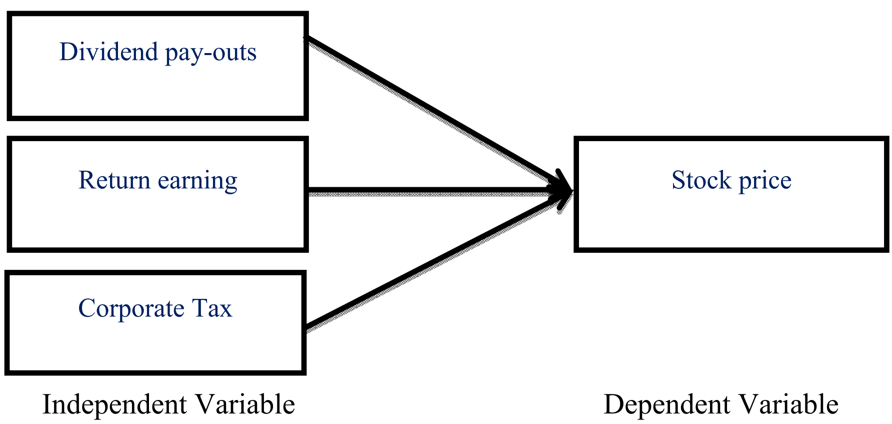
which is distributed on pro rata basis to common shareholders. Akinsulere (2010) viewed stock dividend as the payment of dividend in form of shares.
A study by Isa (2006) using regression analysis from the data generated which found commercial banks' dividend policy to be positively related with their share price even with the introduction of capitalisation as new variable in dividend policy. Attah-Botchwey (2014) found that, as the dividend of companies increase, the share price also increases due to the pressure on the share. This shows that firms with higher dividend payment have their share price going up as well as a result of higher demand of shares. It is recommended that firms should regularly pay dividend as it will cause an increase in the stock market prices, whereas profit retention by firms will result in a decrease in the value of the stock market prices (Sharif, Ali, & Jan, 2015).

Empirical study by Ponsian, et al. (2015) on relationship between dividend policy and share price found that, dividend payout ratio, earnings per share and price earnings ratio have positive relationship while dividend yield is negatively related to share price. Similar study by Machael and Benson (2014) revealed that both dividend payout and retained earnings are significantly relevant in the market price per share of the companies. Another study by Al-Shawawreh (2014) showed significant negative relationship between share price with dividend payout and positive relationship between dividend yield and share price. Other empirical results showed significant negative relationship between share price volatility with two main measurements of dividend policy which are dividend yield and payout (Hashemijoo, Ardekani & Younesi, 2012; Al Masum, 2014).

Fodio (2009) concluded that earnings, previous dividend, cash flow, investment and net current assets have significant aggregate as well as separate impact on the dividend policy of firms quoted on the Nigerian Stock Exchange. Osegbue, Ifurueze and Ifurueze (2014) established no significant relationship between dividend payout in Nigerian banks and corporate performance. Their research outcomes indicate that banks pay dividend in Nigeria with the ability of reducing the agency conflict and maintaining firm's reputation. Hussainey et al., (2011) revealed positive relationship between dividend yield and stock price while on the other hand shows negative association between dividend payout ratio and stock prices.

The theories that will guide this research are the irrelevancy, and the relevency theory of dividend policy. Irrelevancy theory was first suggested by Miller and Modigliani (M & M) in 1961 and said that the payments of dividend are irrelevant and amount paid do not affect the value of the company in the long run. That stockholder wealth is unchanged when all aspects of investment policy are fixed and any increase in the current payout is financed by fairly priced stock sales. They also argued that an active dividend policy should be pursued as a means of maximising shareholder's wealth. They argued that in a tax-free world, shareholders are indifferent between dividends and capital gains, and the value of a company is determine solely by the earning power of it assert and investment. The proponent of the relevency dividend theory by James and Gardon (1959) argued that dividend were all that mattered in the determination of share price base on the fundamental theory of share values. He stated that investors may prefer present dividend instead of future capital gains because the future situation is uncertain even if in perfect capital market. Indeed, he explained that many investors may prefer dividend in hand in order to avoid risk related to future capital gain. He also proposed that there is a direct relationship between dividend policy and market value of share even if the internal rate of return and the required rate of return will be the same.

This study investigated three (3) major determinants of stock prices, namely; dividend payout, retained earnings and corporate tax. These variables were identified based on previous literature by Isa (2006), Fodio (2009), Lashgari and Ahmadi (2014), Sharif, Ali and Jan (2015), which was related to the determinant of stock prices.



2.1 Dividend Payout and Stock Price

Jecheche (2012) found that dividend policy measures (dividend yield and payout ratio) have significant impact on the share price volatility. The study by Amuche (2014) revealed that the dividend yield, earnings yield and payout ratios are a not factor that influences stock prices. Hussainey et al., (2011) found negative relationship between dividend payout ratio and stock price changes. Another similar study by Habib, Kiani and Arif Khan (2012) found dividend yield and share prices to be positively related while payout ratio is negatively related to share price. Dividend Payout Ratio has a significant positive relationship with Share Prices as supported by the Bird in hand theory (Sharif, Ali, & Jan, 2015). Fodio (2009) found significant positive association between dividend payout and dividend policy of firms quoted on the Nigerian Stock Exchange. Ashamu, Abiola and Bbadmus (2010) and Zakaria, Muhammad, and Zulkifli, (2012) found that payout ratio significantly affect the changes in the value of the company. Based on the above evidence the following hypothesis was formulated

H1: ***There is a significant relationship between dividend payout and stock prices of the Nigerian listed banks***

2.2 Retained Earnings and Stock Price

The Modigliani-Miller Theorem states that shareholders are indifferent to the division of retained earnings into dividends and new investments. It predicts that the amount of retained earnings spent on dividends, which raise stock prices, is offset by the effect of issuing new stock to replace the money spent on dividends, which lowers stock prices. The model doesn't consider the use of debt instead of new stock issuance (Eric, 2012). Sharif, Ali and Jan (2015) found an insignificant relationship between retained earnings ratio and share market prices. Fodio (2009) indicated that, the current earnings have significant impact on the dividend policy of quoted firm in Nigerian Stock Exchange. Michael and Benson (2014), Isah (2006) revealed that retained earnings are significantly related to the market price per share. Lashgari and Ahmadi (2014) found insignificant association between earning volatility and stock price volatility. Zakaria, Muhammad, and Zulkifli, (2012) found dividend yield, and earnings volatility to be insignificantly related to the changes in the company's share prices. The result of the empirical study carried out by Salman, Lawal and Anjorin (2015) revealed that the earning streams of companies in Nigeria have a greater impact than their dividend payouts in shaping the price of their shares in the market. Gul et al. (2012) revealed that retained earnings have insignificant effect on market value of equity. Based on the above evidence the following hypothesis was formulated

H2: ***There is a significant relationship between retained earnings and stock prices of the Nigerian listed banks***

2.3 Corporate Tax and Stock Price

Income distribution and capital gain have different tax implications for investors. This will affect the dividend and retained earnings of the firms. Hence the marginal rate of tax of the dormant shareholder can be an important consideration in determining dividend policy (Adediran & Alade, 2013).Taxes provide incentives or encourage for firms to confirm report accounting income to tax incentives because court decisions on reporting method serve as precedents for tax approach. Tax, their incentives for a profitable business with taxable income to differ income to reduce the present value of taxes (David & Gallego, 2009). Company Income Tax as a measure of taxation on the influence on the ability of Nigerian banks to pay dividend (Osegbue, Ifurueze & Ifurueze 2014). Al Masum (2014) found profit after tax to be negatively insignificant in relation with stock prices. Based on the above evidence the following hypothesis was formulated

H3: ***There is a significant relationship between corporate tax and stock price in the Nigerian listed banks***

3. MATERIAL AND METHOD

The ex-post facto research designs are employed in this study. The Ex-post facto research design considers a research problem in which the independent variables have already occurred and with the observation of a dependent variable in retrospective for their possible relations to, and effects on, the independent variable(s) (Asika, 2009).The target population under this study comprises all the twenty-one (21) commercial banks quoted on the Nigerian stock exchange (NSE) market (Appendix 1). This set of requirement allows only banks with strong capital base to be enlisted on the security market. In conducting this research, secondary sources of data was used through the use of annual report and account of the sampled banks and NSE fact book. For the purpose of this study, purposive sampling method is used to represent the entire population in order to ease the research work. The sample size was eighteen (18). The banks were selected based on the availability of data covering the years under consideration. The technique of data analysis adopted for this study is multiple regression analysis. This technique is used because the investigator is trying to examine the significant relationship of certain independent variables: (dividend payout, retained earnings and corporate tax) over another dependent variable: stock price. The data in this research will be analysed using Statistical Package for Social Sciences (SPSS), version 21.0.

3.1 Measures

3.1.1 Stock Market Prices

Stock dividend per share of a firm is defined as total stock dividends divided by the number of outstanding shares. This variable is used as a dependent variable. Stock market prices can be calculated through the process of considering closing market prices of shares (Sharif, Adnan Ali, & Jan, 2015).

3.1.2 Dividend Payout Ratio (DPR) Measure

Dividend payout ratio measures the percentage of profits distributed by the company among shareholders out of the net profits. Dividend payout is considered in this research because it takes consideration of dividend payout and dividend retention rather than dividend per share (Osegbue, Ifurueze & Ifurueze, 2014). Dividend payout ratio is the relative amount of profit distributed by any firm in the form of dividends to the total amount of net income of any business. Dividend payouts ratio may be calculated through following formula.

DPR=Dividends/Net Income

For computing this variable, the sum of cash dividend paid to common shareholders is divided by the net income after tax for each year. It is calculated based on following formula:

$$\text{Payout ratio} = \frac{\text{Dividend Per Share}_{it}}{\text{Earnings per Share}_{it}}$$

EPS_{it} = Earing per share for firm i in year t

Dps_{it} = Dividend per share for firm i in year t

3.1.3 Retained Earnings Measure

Retained earnings are the amount out of the total earnings of the firms that is not distributed as a dividend to the shareholders is utilised by the firm for the purpose of growth. This amount kept by the firm for the purpose of reinvestment in the same firm. This variable is used as an independent variable (Sharif, Adnan Ali, & Jan, 2015). Retention ratio of any firm can be calculated using the following formula; (Net Income-Dividends)/Net Income

3.1.4 Corporate Tax Measure

Taxes provide incentives or encourage for firms to confirm report accounting income to tax incentives because court decisions on reporting method serve as precedents for tax method. Tax, their incentives for a profitable firm with taxable income to differ income to reduce the present value of taxes. Corporate tax is a compulsory payment made by companies to the government out of their profit after deducting all relevant expenses allowed, relief and allowances. The actual tax paid as shown in the balance sheet will be used to measure the variable (Web, 1994).

3.2 Model specification

In order to look at the effect of dividend policy and stock prices, this study follows multiple regression analysis. The dependent variable stock price is regressed against three independent variables that are dividend payout ratio, retained earnings and corporate tax. The following multiple regression equation would be adopted to develop a relationship between the three variables and stock price.

$$SPrices_t = f\,(\beta_1 Dpayout_{it} + \beta_2 REarinings_{it} + \beta_3 CTax_{it,}) \ldots\ldots\ldots\ldots\ldots\ldots 1$$

$$SPrices_{it} = \beta o + \beta_1 Dpayout_{it} + \beta_2 REarinings_{it} + \beta_3 CTax_{it} + \mu_{it} \ldots\ldots\ldots\ldots\ldots 2$$

Where;

$\beta_1 DPR_{it}$ = Dividend payout ratio,

$\beta_2 RE_{it}$ = Retained Earnings

$\beta_3 CTax_{it}$ = Corporate tax

μ_{it} = Error term in the equation or the amount which account for other possible factors that could influence SPrices that are not captured in the model

β_1, β_2, and β_3 are coefficient of investigation of stock price. It depicts the degree of the stock prices by applying the independent variable (dividend payout, retained earnings and corporate tax).

4. RESULTS AND DISCUSSION

This section presents the result of data analysis and tests of the hypotheses formulated earlier in this study. First, descriptive statistics, followed by the regression result are presented and analysed, and then recommendation will be drawn from the findings of the study.

Table 1: Descriptive Statistics

	Minimum	Maximum	Mean	Std. Deviation	Skewness	Kurtosis
Stock Prices	0.70	3.00	0.7762	0.33137	1.233	5.227
Dividend Payout	0.05	0.90	0.3304	0.15704	1.222	4.356
Retained Earning	4.62	12.0	8.8173	0.76123	0.813	0.314
Corporate Tax	0.33	5.45	7.8890	1.98096	-1.38	5.533

Extracted from SPSS output

From Table 1, the mean value for stock prices is 0.77 and 0.33 for the dividend payout of the banks, while retained earnings, corporate tax was having an average value of 8.81 and 7.88 respectively. The minimum value for stock price is 0.70 while the maximum is 3.00, while retained earnings and corporate tax are having minimum value of 4.62 and 0.33 and also having maximum of 12.0 and 5.45 for retained earnings and corporate tax respectively. Dividend payout and corporate tax are among the explanatory variables that recorded a minimum value. This occurred because in some certain years some of the banks neither gained profit nor pay tax. It is observed that the corporate tax has the highest standard deviation of the independent variables that are significant at 5% level and therefore it shows that the corporate tax has the least contribution to the dependent variable (stock price). While, on the other hand, dividend payout has least value for standard deviation and it thus signifies its highest contribution to the endogenous variable of the study. The skewness values of the variables were all close to 0 and 1, the data is considered to be tolerably mild and normally distributed.

Table 2: Regression Result

Variable	Coefficient	t- statistics	Prob.
Dividend Payout	5.5344	1.7572	0.0342 **
Retained Earning	12.6567	4.7740	0.0000 ***
Corporate Tax	-4.3946	-0.7942	0.0232
R- squared	0.7724		
Adjusted R- squared	0.7389		
F- statistics	203.3282		
Prob. (F- statistics)	0.0000		
Durbin-Watson Stat	1.2641		

Notes: *p<0.1, **p<0.05, ***p<0.01

As revealed from table 2, dividend payout had positive significant effect on commercial banks' stock prices (coefficient of DPR = 5.5344; p-value = 0.0342). Also, for the retained earning variable had positive significant effectt on stock prices of Nigerian listed commercial banks (coefficient of REarnings = 12.6567; p-value = 0.000), while corporate tax had negative and significant effect on commercial banks' stock prices in Nigeria (coefficient of CTax = -4.3946; p-value = 0.0232). The coefficient of determination of R-square (R2) indicates that 77.2% of the variations observed in the dependent variable were explained by variations in the independent variable. The adjusted R2 is 0.738 that is 73.8%, indicating that the dependent variable was explained in variations in the independent variable. Thus, the Adjusted R2 shows that dividend payout, retained earnings and corporate tax accounts for 73.8% of the variation of the listed commercial banks' stock prices in Nigeria. However, the Durbin-Watson statistics which is 1.26 indicates that there is no autocorrelation in the model.

The finding of this study supports many other studies in this area for example, Isa (2006), Fodio (2009), Okafor and Mgbame (2011), Adediran and Alade (2013), Amuche (2014), Machael and Benson (2014) and Osegbue, Ifurueze and Ifurueze (2014) which show significant effect between dividend payout, retained earnings and stock prices. The result is also consistent with the finding of Al Masum (2014) which found profit after tax to be negatively insignificant in relation to stock prices. While the result of this study is inconsistent with the findings of Habib, Kiani and Arif Khan (2012), Lashgari and Ahmadi (2014), Zakaria, Muhammad, and Zulkifli, (2012) and Gul, et al. (2012) which found negative insignificant effect between earning volatility, dividend payout and stock price.

5. CONCLUSION AND RECOMMENDATION

The results of this study show that dividend payout, retained earnings have significant relationship with stock Market Prices. The study also revealed that corporate tax has significant negative relationship with Stock Prices of the listed banks in Nigeria. The result indicates that the coefficient of correlation (R) between the independent variables and the dependent variable has been statistically significant. This means that if listed commercial banks in Nigeria increase their dividend payout ratio, maintain their retained earnings, it will have a positive impact on their stock prices. The result also revealed R2 of 0.77 which is significant. This implies that the independent variables (dividend payout, retained earnings and corporate tax) strongly explained the variance in the dependent variable (stock prices of listed commercial banks in Nigeria). Therefore dividend policy has impact on the value of stock prices in the listed commercial banks in Nigeria. Since the commercial banks dividend policy affects their prices in Nigeria, banks should introduce the system of paying the dividend semi-annually. This will cause an increase in the stock market prices and will generate confidence of the shareholders and potential investors of the stock market. This is because the study found that the dividend policy control more than 75% of the variance in the stock prices of listed commercial banks. This study also recommends that adherence to interest of shareholders in choosing dividend policies that will maximise shareholders' value by management.

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Appendix-A

Table 3: The Population of the Study

S/No	Name of Banks	Year of incorporation	Year of listing
1.	Access Bank Nigeria Plc.	1989	1998
2.	Citibank Nigeria Limited	1959	1993
3.	Diamond Bank Nigeria Plc.	1999	2005
4.	Ecobank Nigeria Plc.	1986	2006
5.	Enterprise Bank Limited	2006	2006
6.	FCMB Plc.	1982	2004
7.	Fidelity Bank Plc.	1987	2005
8.	Standard Chartered Nigeria	1999	2006
9.	First Bank Of Nigerian Plc.	1969	1971
10.	Guaranty Trust Bank Plc.	1990	1996
11.	Stanbic IBTC Chartered Bank Plc.	1989	2005
12.	Heritage Banking Company Limited	1989	2003
13.	Keystone Bank	2011	2011
14.	Skye Bank Plc.	1999	2005
15.	Mainstreet Bank Limited	2011	2011
16.	Sterling Bank Plc.	2006	2006
17.	United Bank For Africa PLC	1961	1971
18.	Union Bank Of Nigeria PLC	1969	1970
19.	Unity Bank Plc.	2005	2005
20.	Wema Bank Plc.	1945	1991
21.	Zenith Bank Plc.	1998	2004

Note: This table presents the list of the banks that are listed on the NSE.