

Dividend Payout Decision and Investors' Behavior

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Abstract

The paper aims to examine the effect of dividend payout on perceived value of shareholders. The purpose behind of this study is to understand awareness of investors about dividend payout and investment behavior. This study is based on descriptive research design. It is based on the perception of investors and includes the questionnaire asked to 150 investors at Kathmandu Valley. It is found that investor's preference for investment lies in dividend payout of the organization as investors are positively influenced through dividend distribution. Companies must maintain stable dividend payout ratio as shareholders expect it and reveal a preference for it. As an investor, one must be aware of dividend stock for the stable profit for longer period of time. Such stocks can act as hedges against higher-risk if there is any other risky stock in the portfolio.

Keywords: Dividend Payout, Investors, Behavior, Shareholders

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Introduction

Dividend is defined as a return or reward from investment in equity shares. The profit made by the firm which is distributed to the shareholder is termed as dividend. Every firm after making profit either retain the cash for further investment or distribute it among the shareholders. The firm should decide whether to carry on the money as retained earnings or pay the dividend. It may be in cash, share or combination of both.

As per the Fama (1970, 1971), Efficient Market Hypothesis (EMH) suggest that market price always absorb all the information and reflect in

price without bias. In this efficient market, prediction of price movement is difficult task however understanding perception of shareholders about dividend distribution of company adds value for individual in the selection of stocks. Each individual looks for certain profit out of his/her capital investment. Dividend in this form is a reward paid to the shareholders for their investment in a company's equity. Dividends are payments made by a corporation out of its profit to its shareholders. In other words, the dividend is that portion of earning, which is paid to the common stockholder, as a return on their investment. When a corporation earns profit, such money can be used

either in the form of reinvestment in the business or it can be paid to the shareholder as a dividend. Mostly the corporations retain a portion of their earnings and pay the remainder as a dividend. Firms use such retained earnings to provide funds for long-term growth; which is also known as internal source of financing.

As such, there are two different understanding about immediate return and future return as in the form of retained earnings. In dividend distribution, shareholders can enjoy current return whereas in retained earnings shareholders can see future prospects as in investment opportunities, growth and tax advantages in retained earnings. Here in Nepal, for taxation purpose, there is no provision to pay tax in retained earnings until it is realized. Basically, this study is concerned with the effect of information about dividend policy. As per the signaling theory, there is association of the dividend content information hypothesis impacting on the market. It holds that dividend policy acts as a vehicle for transmitting information from firm's authority to the market. With this, the main focus of this paper is to examine the viewpoint of shareholders upon dividend payout policy of the organization in the context of Nepal.

Review of Literature

Most of rational investors believe on knowledge of finance, as a most influencing tool to apply for the optimal and rational decision-making. However, recent studies have highlighted the behavioral phenomena of the investors' psychology relating with perceptions, memories, and thoughts without awareness etc. As such Baker and Nofsinger (2010) opined that investor's thoughts and feelings can change the decision-making process from rational to irrational.

In the South Asian context, considering Nepalese

and Indian stock markets employing variance ratio, Dangol (2011) examined the random-walk behaviour and weak form of market efficiency. The study found that the variance-ratio tests were rejected the random-walk hypothesis for both countries' stock market. There are past studies highlighting significant efforts of the factors of investors' representativeness behaviour. For example, Toma (2015) found the positive effect of representativeness bias on investment-decisions. In this context, author opined that representativeness bias is the main cause to increase individual investors' returns. In another study, Badshah, Irshad and Hakam (2016) also found a positive relationship between investment decisions and representativeness bias. Furthermore, Ikram (2016) showed that representativeness bias positively affected individual investors' trading behaviour.

With this viewpoint, investors' behavior upon dividend decision is important part for the study. Dividend policy, in practice, is primarily concerned with the choices regarding dividend payout and pattern of payment and retention. It's a choice that considers the quantity of profits to be retained by the corporate which to be distributed to the shareholders. This policy is one of the most important financial policies not only from the viewpoint of the corporate, but also from all other stakeholders such as shareholders, the consumers, employees, regulatory bodies and the Government. For a company, it is a pivotal policy around which other financial policies rotate (Alii et.al., 1993).

Dividend is desirable for the shareholders, which inspires them for the further investment on company's shares. Dividend payout decision is an important aspect of financial management because it determines the division of earnings between payment to stock holder and reinvestment in the firm to exploit growth opportunities. It affects the value of the firm as well as overall financing

decision such as financial structure, the flow of funds, corporate liquidity and investor's satisfaction.

Research Gap

As in efficient market theory, market quickly impounds publicly available information, including dividend payout decision, and other important information that might be used to predict stock prices. In stock market, the term efficiency indicates is the market in which relevant information is impounded into the price of financial assets. The theory of efficient markets is concerned with stock prices at any point in time fully reflect available information (Fama, 1970). In efficient market, shareholders are assumed as an intellect buyer as they reflect stock understanding in their purchase behavior.

There are number of empirical tests (Pettit, 1972, 1976, Aharony & Swary, 1980,) have shown that dividend changes announcements are positively associated with share returns in the connection with the dividend change announcements. This finding indicates on existence of dividend information content, or signaling effect. Although, these studies were held in developed countries on the impact of dividends announcement on stock price and most results showing significant role in stock price, there observed need of such study in the context of Nepal. So, this paper focuses on understanding investors' perception about dividend payout information of the organization.

Research Objectives

Dividend policy of a firm is a guideline for dividing its net earning into two parts; the retained earnings and dividend payment. The optimal dividend policy of a firm depends on investor's desire for capital gains as against income, their willingness to decline dividend now for future returns and their

perception of the danger related to the postponement of returns. Miller and Modigliani (1961) assumed dividend irrelevance theorem a lower dividend payouts ratio was to be related to higher future growth and thus higher future equity returns. In what over so, Dividend distribution policy and retain earning are the most important decision for today's managers. Dividend distribution is vital financing decision that involves with the payment to shareholders in return of their investments. Within the context of above discussed issues, the main objective of this study includes:

- To examine the effect of dividend payout on perceived value of shareholders?

Methods

This study is based on descriptive research design. Survey was made with 200 people, out of which 150 people responded the questionnaire, resulting response rate as 75 percentages. This study is based on a sample of 150 investors who were available for the responses within Kathmandu Valley. Investors had been identified and selected according to the following criteria: age ranged 18–62 years old (b) investing for at least one year prior to the data collection to be oriented about dividend payout and more about share market knowledge (c) able to express opinion about interest of share market and feel ease for the response in survey.

The data related to the factors of dividend policy have been collected through questionnaires and the mean values for each of the factors had been calculated. Since a 5 point Likert scale had been used for the collection of the data, the mean greater than or equal to 3 has been interpreted as an acceptable statement for different of the factors of a dividend policy.

Analysis & Discussion

Demographic characteristics of the sample:

Here, personal and occupational factors such as

age, gender, occupation of the respondents and income level of respondents were presented as follows.

Table 1
Demographic characteristics of the sample

Attribute	Characteristics	N	%
Age	Below 25	33	22
	25 to 50	107	71
	Above 50	10	7
Gender	Male	115	77
	Female	35	23
Occupation of the respondents	Public	17	11
	Private	94	63
	Self employed	39	26
Income of respondents	Below 25,000	71	47
	25,000 to 50,000	52	35
	Above 50,000	27	18

In this study, the age range below 25 was 22% (n=33), between 25 to 50 age was 71% (n=107), and 50 and above years was 7 % (n=10). It is interesting to note that a large portion of the respondents are in 25 to 50, showing the demography active in share market as in mid career age. As per the gender, 77% (n=115), are male whereas female are 23% (n=35), the highest percentages of respondents are male. Similarly, in occupation, 11% (n=17), are in public occupation, 63% (n=94), are in private occupation and 26% (n=39), are self employed. According to the income of the respondents, 47 % (n=71), have monthly income below Rs. 25,000, 35% (n=11),

have income between Rs. 25,000-50,000 and 18% respondents have income more than Rs. 50,000. Higher percentages of monthly income are seen below 25,000 and higher occupations from private sectors show that people are looking extra money from share investment.

Subjective factors

Number of opinion, marking answer of the question to what extent does the dividend policy affect the market prices per share are presented as in table 2.

Table 2
Dividend policy and market price

S.N	Particulars	Frequency	Percentage
1	High	59	39
2	Medium	78	52
3	Low	13	9
	Total	150	100

Table 2 shows that out of 150 respondents, 39% says the dividend policy highly affects the market price per share. 52% says the dividend policy moderately affects the market price per share and 9% respondents say that the dividend policy has

less or low affects in the market price per share. The highest percentage of result under medium level indicates that people assumed it as positive signaling on the market price of the stocks.

Table 3
Inspiration for investment

S.N	Particulars	Frequency	Percentage
1	Lack of alternative investment	47	31
2	Expectation of higher prices in Future	54	36
3	Future benefits from the institution	39	26
4	Others	10	7
	Total	150	100

Table 3 shows that out of 150 respondents, 31% says due to lack of alternative investment opportunity, people are interested to invest in the shares through primary and secondary market. 36% says expectation of higher prices in future inspired them to invest. Similarly 26% of

respondents are motivated to invest in the shares in secondary market because of future benefits from the firm and only 7% respondents are motivated by other factors to invest. The highest percentage holds expectations of higher prices in future.

Table 4
Awareness of financial condition of the organization

S.N	Particulars	Frequency	Percentage
1	Yes	126	84
2	No	24	16
	Total	150	100

Table 4 shows that out of 150 respondents, 84% of respondents are aware of the financial condition of the institution and 16% of respondents are not aware of the financial condition of the institution

while investing in the shares. Results show that the highest percentages of respondents were aware of the financial condition of the institution while investing.

Table 5
Motivating Factors in investment

S.N	Particulars	Frequency	Percentage
1	Dividend	59	39
2	Earnings per share	49	33
3	Right Share	33	22
4	Others	9	6
	Total	150	100

Table 5 shows that out of 150 respondents, 39% of respondents are inspired by the dividend of the institution to invest in secondary market, 33% are inspired by the earning per share of the institution to invest in secondary market, 22% are inspired by right share of the institution to invest in secondary

market and only 6% are inspired by other factors of the institution to invest in secondary market. The highest percentage of respondents is inspired by the dividend payout of the institution to invest in secondary market.

Table 6
Understanding about dividend practices

S.N	Particulars	Frequency	Percentage
1	Payment of regular dividend	60	40
2	Paying irregular dividend	32	21
3	Both	58	39
	Total	150	100

Table 6 shows that out of 150 respondents, 40% says payment of regular dividend practices is followed by banks in Nepal, 21% says paying irregular dividend practices followed by the banks in Nepal and 39% says both regular and irregular

dividend practices followed by the banks in Nepal. The highest percentage opined about the payment of regular dividend practices followed by listed companies in Nepal.

Table 7
Options preferred in dividend

S.N	Particulars	Frequency	Percentage
1	Pay from reserve	65	43
2	Pay stock dividend	42	28
3	Pay no dividend at all	43	29
	Total	150	100

Table 7 shows that out of 150 respondents, 43% respondents suggest the company to pay from reserve if the company has not gain profit to pay dividends, 28 % suggest the company to pay stock dividend if the company has not gain profit to pay

dividends and 29% suggest paying no dividend at all if the company has not gain profit to pay dividends. The highest percentage of respondents suggests the company to pay from reserve if the company had not gain profit to pay dividends.

Table 8
Perceived risk

S.N	Particulars	Frequency	Percentage
1	Very High	24	16
2	High	25	17
3	Normal	101	67
	Total	150	100

Table 8 shows that out of 150 respondents, 16% rate the risk factor as very high in the share market, 17% rate the risk factor as high in the share market and 67% rate the risk factor as normal in the share market. The highest percentage of respondents perceived share market as not risky one.

Investors buying behavior

Investors' behavior is psychological issue that can be observed for why people buy or sell stocks. Factor focusing upon how investors interpret and act on information to make investment decisions are presented in Table 9.

Table 9
Investment Buying Behavior

Subject of the Question	N	Mean	S.D
Before I invest I carefully consider whether I can afford it.	150	3.71	1.445
I find it more satisfying to invest money in share than to save in bank.	150	3.69	0.94
Income level has direct relation in raising investors' interest towards financial instrument	150	3.58	1.232
Investors have sufficient information regarding dividend policy of companies	150	3.24	1.156
Dividend payout provide signal to prospective investors	150	3.61	1.014
Do you think that a firm should strive to maintain uninterrupted or a steady dividend payment	150	3.49	1.049
Investors discriminate between dividend paying and not paying companies	150	3.57	1.103
Investors prefer long-term investments rather than short-term investments	150	3.46	1.243
Do you think that the market uses dividend announcements as information for assessing firm values	150	3.76	1.248

Table 9 shows investors' buying behavior upon stock's purchase. The mean value for the question "before I invest I carefully consider whether I can afford it" was 3.71 which is greater than 3 that can be interpreted as respondents carefully considered whether they can afford to invest or not. Here, respondents only invest in those shares which they can easily afford in the market. The mean value for the question "I find it more satisfying to invest money in share than to save in bank" was 3.69 which is also greater than 3 and can be interpreted as respondents are more satisfying to invest in shares than to save money in the bank.

The mean value for the question "Income level has direct relation in raising investor's interest towards financial instrument" was 3.58 which is greater than 3 and can be interpreted as there is direct relation between investors income level and raising investor's interest towards financial instrument. The mean value for the question "investors has sufficient information regarding

dividend policy of companies" was 3.24 which is greater than 3 and can be interpreted as investors has sufficient and necessary information relating to the dividend policy of the company which will help them to investment. The mean value for the question "Dividend payout provide signal to prospective investors" was 3.61 which is greater than 3 and can be interpreted as signal to the prospective investor are provided by dividend payout. The mean value for the question "Do you think that a firm should strive to maintain uninterrupted or a steady dividend payment" was 3.49 which is greater than 3 and can be interpreted as firm should strive to maintain uninterrupted or a steady dividend payment.

The mean value for the question "Investors discriminate between dividend paying and not paying companies" was 3.57 which is greater than 3 and can be interpreted as investors discriminate between dividend paying and not paying companies. The mean value for the question

“Investors prefers long-term investments rather than short-term investment” was 3.46 which is greater than 3 and can be interpreted as investors prefer long-term investments rather than short-term investment. The mean value for the question “Do you think that the market uses dividend announcements as information for assessing firm values” was 3.76 which is greater than 3 and can be interpreted as the market uses dividend announcements as information for assessing firm values.

Dividend Payout Ratios: Trend Analysis

As a part of understanding dividend payout ratio and pattern, overall banking sectors' dividend payout trend analysis was performed so as to make assessment of financial health of banking sector. The study examined the past performance of banks in terms of dividend payout ratios to determine how they perform in the different year and economic situation.

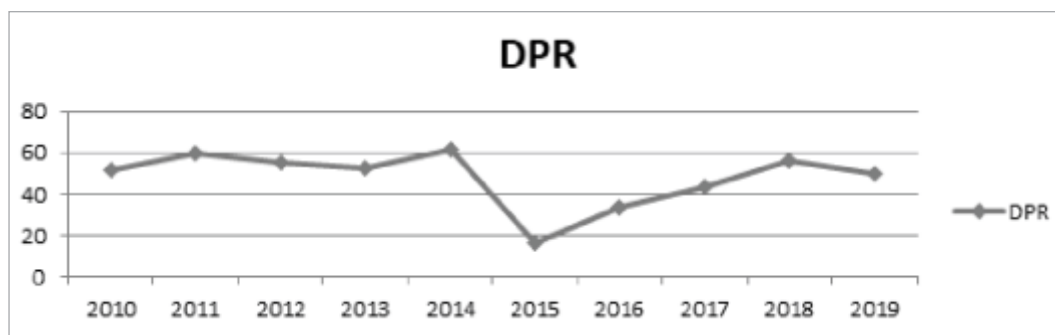


Figure 1. Trend Analysis of Dividend Payout Ratio

Figure 1 shows that there is increase in dividend payout in 2011 and gradually it decreases in 2012 and 2013. Highest DPR is in 2014. Just after it, 2015 year marks with the lowest dividend payout ratio. From 2016 onward, there was increasing rate in dividend payout till 2018 then again in 2019, DPR is decreasing. Almost this figure implies that currently Nepalese commercial banks are distributing good amount of cash dividends to their shareholders.

Research Findings

Mostly people buy stock only when they assume that the price of stock will rise in future and help them earn a profit. Similarly, they sell their stocks either to book the profit or manage their losses when they feel that prices will fall in the future. Investors, in our context, mostly depend upon market sentiments as we can observe that most of the investors, in Nepal, are highly influenced by haunch, rumors, news and speculation. In the

context of developing nation like Nepal, political environment and political stability play vital role in the fluctuation of share price. Such fluctuations in stock prices can be observed through fundamental analysis, technical analysis, and market sentiment analysis. Above demographic analysis, opinion expression remarks about sentiments, attitudes and expectation of investors which ultimately affects share prices. As per the finding, herding behavior and market sentiments have higher impact in share price than fundamental and technical factors.

Conclusion

As a conclusion part of the study, investor's preference for investment lies in dividend payout decision of the organization as investors are positively influenced through dividend distribution. Generally, Corporate generally favor a stable dividend payout ratio as shareholders expect it and disclose a preference for it. Shareholders want a stable rate of dividend

payment. Risk avoiding shareholders are willing to invest only in those companies which pay high current returns on shares. In the same line, market uses dividend announcement as information for assessing firms' values. In this study, we find that the socio-economic characteristic, risk profile, and investment awareness positively influence future stock market investment decisions that is consistent with the findings of earlier studies (Dimmock and Kouwenberg, 2010; Rooij et al., 2011). Furthermore, in terms of Market, the Nepalese stock market has a system of adjustment so that it adjust price in an efficient manner as per new dividend information according to the dividend changes on certain time interval.

Recommendations

In efficient market, every firm operating in a capital market follows some sort of dividend payment pattern. It is the way to fulfill the aim of the shareholder for maximizing their wealth through the dividend. However, considering investment and market pattern, it seems that there may be lack of awareness; inadequate knowledge, and information, as people are haphazardly investing in shares. Personally, an investor must be aware and upgrade financial knowledge and awareness. For those who are aware in market, dividend is one of the most important factors to consider in investment decision in stock market. From organizational part too, it is an effective way to attract new investors, maintain present investors and controlling position of the firm.

In the context of Nepal, most of the investors are interested to have the stock which is offering dividend and stock within certain span of time. Really, dividend distribution is the sign of sustainability of the company. As we can feel trust of the company that provides regular dividend so considering dividend as prime in investment or dividend investing is often considered as a low-risk

strategy. However, one should not commit the mistake of buying dividend stocks and forgetting for a year or longer. The problem is that, like valuations of stocks, and change in organizational efficiency that can be observed in quarterly performance, may bring changes in dividend policy of the organization. Finally, as an investor, one must be aware of dividend stock for the stable profit for longer period of time. In the selection of script, high-dividend stocks should be included somewhere in the portfolio. Such stocks can act as hedges against higher-risk if there is any other risky stock in the portfolio.

Limitations

This study is based on basically primary data and limited number of participants so it may not reflect to replicate same findings in other context.

Scope for Future Research

The dividend announcement has significant role in Nepalese capital market. However, in the part of the form of market efficiency and its impact, there requires furthermore studies and test so that it can helpful to reflect in the security price.

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