IMPACT OF DIVIDEND ANNOUNCEMENTS ON SHARE PRICE OF SELECTED LISTED COMPANIES AT KSE

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ABSTRACT- *The finance department has important role in all levels of decision making, the capital structure is effected by all the decisions particularly dividend decisions. Because these decision bring drastic change in the cash flows, financial structure, and corporate liquidating behavior of investor against the dividend announcement. There is correlation between dividend and value of share. Some funds managers are convinced that dividend should be given but other are of the view that earrings should be retained for future business opportunities. The finance manager has to convince himself that either he should distribute the profit or retained it. This study focuses on the impact of dividend announcement of listed companies at Karachi Stock Exchange. Which is the biggest equity market in Pakistan. The empirical result has shown that after the announcements of dividend the stock prices tend to be effected significantly. They explain that the result as consistent with previous studies. Total number of cash dividend paying companies are 63 listed at KSE with 2 dividend announcements are seen. This study indicated that the relationship between the share price of listed companies and cash dividend payment. Most of the companies distribute dividend in shape of stock dividend. The study also showed that is significant change in the market price of share before and after the dividend declaration and payment is taken place. The empirical evidence shows that there was a significant change in share price of sampling companies of this study before and after dividend declaration.*

INTRODUCTION

In 1990s, Pakistan has launched liberal fiscal and monetary policies. In the light of these policies, many sectors of the economy such as banking, energy, chemical, cement were privatized. The objective was to create competitiveness and efficiency so that Pakistan can compete in international markets [1]. Pakistan's strategy was to grow through international standards with the help of other developed nations. The advancement of a nation demands enlargement of creative and dynamic activities, which convert in the consequences of capital realization that is the wealth of the country. The change in the wealth of the county is known as asset of the country. Asset is the key source of wealth creation. Capitalist requires to earn profit from the investment he made. This is major motive behind every investment activity. No profit means no investment. Capital will block if there is no profit or growth in the capital. The investors need two type of return from the investment, one is capital gain, and other is the dividend. In the capital market, everyone wants these two types of returns after making investment [2].

Shareholders also make investment in the hope of these two types of returns, they can increase their investment from these two sources of growth and wealth creation. When the company generates profit, it will have to decide whether profit should be re-invested in the business, or distributed among shareholders of the organization in the shape of dividend. Dividends are the payment to be made to shareholders from a firm's profit in return to their capital invested in the business [3].

In financial management, there is crucial desire to maximize the stockholder's wealth. For this purpose, the finance manager has to decide about the profit, whether it should be retained as re-invest in the capital of the business or given it in shape of dividend. This is known as dividend policy. But mind it decision should be in the favor of the shareholder of maximization of wealth. Among all the features of dividend policy, the finance manager has to see what the magnitude of earnings is, how much profit should be distributed among the shareholders, and how much money should be retained for future business expansion. [4].

Previous year earning is put in the account as retained earnings. Retained earnings are used to pay dividend or making further investment in the profitable projects. Re-investment enhances firm's profit and earning. This leads to increase the main phenomenon of maximization of shareholder's wealth. But it is provocative that how much earning should be distributed as dividend and how much be retained. The answer should be in best interest of shareholders. The Board of Directors and management is also apprehensive about the organization that affects the welfare of the stockholders. The welfare can moderately be determined by the dividend received; more precise decision is the market value of the share. In the point of the shareholders, dividend yield is less risky than capital gain. Dividend is the payment which is made to shareholders out of residual profits. So the corporate profit or surplus, that has two uses: it can be re-capitalized in the organization's capital structure or it can distribute to stockholders in shape of dividend. Most of the organizations have the priority at first to re-invest the money out of profit in the projects that they have decided to initiate, then remaining certain sum of money distribute in the shareholders. This strategy is use when the company or management wants to maximize the shareholder's wealth [5].

Even though organizations do not have the commitment to announce dividend on their ordinary stocks, they are in the ordinary course of time unwilling to revise their rate of dividend payment according to the hopes and needs of the stockholders. Rather they have the strategy to retain the profits, re-invest them in profitable venture, giving impression to their investors that company will pay more dividend in future by generating more revenue [6].

In finance, theory of dividend and its impact on the firms' share price is one of the most bamboozling theories. Researchers have indicated certain rules and regulations while making decision regarding dividend announcement decisions. In this way, they can satisfy the stockholders and maximization of firm's wealth.

In the dividend policy, we mean cash payment policy that managers have to decide the magnitude and arrangement of cash distribution among stockholders.

Miller and Modigliani claim that in perfect capital markets, firms value cannot be affected by the dividend announcement decisions. [7]. Nevertheless, many financial experts and most academic scholars are against the above point of the view. In their view, they presented a lot of theories about how the dividend shake organization's value and also given advice to the financial managers how they should treat dividend as policy decisions. Eventually, there are number of factors mentioned in financial literature and they must be keep in mind while deciding about dividend declaration and payment policies. These factors are also called potential determinants for dividend decisions.

In the history of Pakistan, most of the companies pay dividend regularly. It is also noticed that some companies never paid dividend since their listing. It is generally observed that those companies which pay dividend regularly their share prices are increased in the stock market. So it is a matter of fact that announcement and payment of dividend affect the share price positively, but some researchers are of view that the information about the announcement of dividend do not affect the share price. When organization announces dividend, it obvious from management's perspective that there is something added in the value of shareholder's wealth in shape of growth and profit.

1. LITERATURE REVIEW

The book value of share is the ordinary share capital in the balance sheet plus the value of shareholders' reserves. The value is a historical figure which reflects accounting adjustments and procedures. The book value may be very different to the market value of the shares. This is the share price multiplied by the number of shares in issue which reflects investors' expectations of future earnings. There are differing views about share price movements. Those are fundamental analysis theory, technical analysis theory and random walk theory

Efficient market hypothesis (EMH) also attempts to explain share price movements. The ability of stock market to price shares accurately has been tested to see if they correspond to one of three levels of efficiency. Different types of efficiency can be distinguished in the context of the operations of financial markets. Those are allocative efficiency, operational efficiency and informational processing efficiency. There are various features of efficient market hypothesis. These (A) reflect all the relevant information. (B) No individual dominates the market. (C) Transaction cost is not so high as to discourage trading significantly. (D) There are no or low cost of acquiring the information.

Impact of efficiency on the share price may be one of them. (A) If the company makes an investment with a positive net present value, shareholders will get to know about it and the market price of its shares will rise in anticipation of future dividend increases. (B) If a company makes bad investment shareholders will find out and so the price of its share will fall. (C) If interest rates rise, Shareholders will want a higher return from their investments, so market prices will fall.

Efficient market hypothesis asserts that financial markets are "information- efficient." In significance of this, no one can receive returns beyond the limits of standard market returns on a risk-adjusted basis, given the information available at the time the investment is made. In this context, there are three major stories of the hypothesis: "weak," "semi-strong," and "strong." The weak-form EMH asserts that prices on traded instruments (*i.e.*, stocks, bonds, or property) already reproduce all past openly obtainable information. The semi-strong-form EMH asserts both that prices reproduce all openly obtainable information and that prices instantly transfigure to reflect fresh public information. The strong-form EMH additionally claims that prices instantly reflect even concealed or "insider" information. Critics have held responsible the belief in rational markets for much of the late-2000s financial crisis. In response, proponents of the hypothesis are of the view that market efficiency does not mean having no uncertainty about the future, that market efficiency is a simplification of the world which may not always hold true, and that the market is practically efficient for investment purposes for most of the individuals.

This concept was extensively acknowledged until 1990, when behavioral finance economists, who has been an unconventional component, became main branch. It proved that problem with efficient market hypothesis, the stock with low denomination to income, (and same as low denomination to cash flow or book value) leave behind other stocks examined in the empirical studies. Unconventional studies have suggested that rational preference is the main cause theses inefficiencies; most of the investors want to purchase high-priced growth stock instead of value stock. Even though the efficient market hypothesis has become debatable, permanent inefficiencies are detected due to substantial thinking [8].

Fama portrayed the concept of random walk hypothesis in his thesis. Samuelson also acknowledged the account of efficient market hypothesis. Fama launched both theory and confirmation for the assumptions in the 1970s. This is the phase of extension of paper and advancement of the theory that is inclusion of basic definition of three types of financial market efficiencies: weak, semi-strong and strong [8]. The efficient market hypothesis developed as a conspicuous theory in the mid-1960s.Fama's Bachelor's thesis was published in 1963 beside empirical work mentioned above in compilation modified by the Paul Cootner [9].

By the virtue of weak form of efficiency, no one can project future prices by examining only previous year's prices. Historical data cannot help in earning more returns in the long run by using other speculation tactics based on previous prices. By practically analysis, techniques will not be able to produce more returns. Previous share prices do not display sequential enslavement in the determination of future prices. Means to say that future prices arrangements are calculated completely by the information that are not confined in the previous price sequences. Therefore, it must follow random walk. This "soft" EMH does not say that the prices will be in equilibrium but tells that market contestants will not be able to earn significant returns from the market . Therefore, EMH states that all prices movement is non-trending with regard to time passed. As the higher period passed there will be more tendency of correlation between share prices and length of time. Various studies have projected that such non-random prices movement.

The delinquent of algorithmically constructing prices that may replicate all the available information has been mostly studies in the field of computer science. For example, the complexity of finding the arbitrage opportunities in pair betting markets has been shown to be hard.

It is stated that publically available information about the firm's performance put due impact on the share prices of the firm. This anthology is hastily known as semi-Strong form efficiency. More returns can be earned through this information. It is stated that basic and technical methods of analysis are unlikely to produce excessive returns, Third form of efficient market hypothesis is strong-form. In this regard, share prices reveal that public, private information, otherwise no one can earn maximum return if insider information is restricted or banned to get this information and make prediction about the share price in the future. This restriction may be in form of legal exceptions not otherwise.

Generally, in the past there was a so handy relationship between efficient market hypothesis and random walk prototype, second to it Martingale Prototype. This model was first introduce by Jules Regnault, a French broker in 1863 and then this idea was second by Louis Bachelier, a French mathematician in his Ph.D. thesis in 1900. Initially, his work was ignored in "The theory of Speculation". But in the start of 1930 his work was verified through independent research. Now certain research work point out that US stock market and related financial stocks were following the random walk hypothesis. Research studies have indicated that the professional investors were failed to predict the market in 1930s and 1940s.

It is generally assumed that the stock market is "micro efficient" but not "macro inefficient." Numerous researches have been carried out in the prose which is immense facilitate to comprehend the impact of dividend announcement on the share price of the firms. These researches show assorted prototypes of outcome.

Some analysts have criticized the evidence provided by this instant "efficient" response, pointing out that an immediate response is not necessarily efficient, and that the long-term performance of the stock in response to certain movements is better indications [4].

A study on stocks' response to dividend cuts or increases over three years found that after an announcement of a dividend cut, stocks underperformed the market by 15.3% for the three-year period, while stocks outperformed the market by 24.8% for the three years following the announcement of a dividend increase. Encouraging impact of dividend disbursement pronouncement an abnormal returns of stocks has been observed by Gordon [10] Lintner [11] , and Lonie, et al. [12] Foster [13] institute the understanding of investors to increase or decrease dividend and discovered that on the average, abnormal returns of companies even one day before the announcement of dividend were considerably different from zero even for those companies in which there was no change in dividend. In other words, it can be helpful in reducing the agency problems.

2. DATA AND METHODOLOGY

In our research study, there is need to check whether the impact of dividend announcement on the share price of the others sectors like oil and gas, Cement, Fertilizers, Energy, Textile, Chemical and Tobacco etc. We have taken seven sectors of the economy including financial sector. The time span for this research study was 2004-2010.

This study examined daily stock returns around announcements of dividend of listed companies. Applying the same analytical methods used by Bremer and Sweeney and Cox and Peterson, We includes event stocks whose prices are at least Rs.10 per share prior to the event to reduce the possible price reversal induced by bid-ask price bounce. As is typical for the literature, the stock daily abnormal return (AR) is calculated as the difference between the actual daily stock return and the estimated stock return based on the market model estimated over a 21-trading-day pre-event period [21, 21]. Cumulative abnormal returns (CARs) for each stock are formed by aggregating the individual daily stock ARs. Denoting the large price decline event day as day 0, we examined the ARs of 43 trading days [-21, +21], Cross-sectional average ARs and CARs were calculated and tested for statistical significance. Furthermore, we examined whether the post-event abnormal stock returns for the event firm can be explained by prior event firm and industry variables.

The Objective of this study is to investigate the impact of dividend announcements on stock market returns with the help of event study on the dividend announcement date. These announcements relate to announcement of cash dividend & stock dividend. For this study, data of four industrial sectors such as Cement, textile, Oil & Gas, banking and fertilizers has been collected from the Karachi Stock Exchange and Daily Business Recorder. For the period 2004 -2010. A total of 100 dividend announcements during this time period were taken as a sample and their effect was noted on event firms and its rivals. Impact of dividend announcements on stock prices of 21 days before this announcement and 21 days after this announcement has been calculated in this study. Financial techniques such as Average Abnormal Stock returns, Cumulative Average Abnormal Stock returns, are applied for the purpose of analysis of data. Three Statistical tools such as Arithmetic means, Standard Deviation and T-Statistics were to calculate the results. We calculated actual returns for event firms and weighted returns of rivals' portfolios during the same time period. Then average market returns with respect to each specific announcements were calculated in order to measure the abnormal returns of event firms and rivals.

Table 1 Empirical statistics

Day	AAR	SD	CAAR	T VALUE	Day	AAR	SD	CAAR	T VALUE
-21	0.00283	0.03120	0.21548	6.90752	1	-0.00736	0.03426	-0.01595	-0.46551
-20	-0.00167	0.02905	-0.00311	-0.10694	2	0.00301	0.02998	0.00660	0.22006
-19	0.00119	0.03048	0.00233	0.07633	3	-0.00344	0.02452	-0.00768	-0.31315
-18	0.00452	0.02734	0.00533	0.19516	4	-0.00468	0.02208	-0.01014	-0.45896
-17	-0.00387	0.04424	-0.00266	-0.06009	5	0.00245	0.01914	0.00535	0.27936
-16	0.00536	0.04874	0.00743	0.15238	6	0.01043	0.08678	0.02286	0.26348
-15	-0.00135	0.05052	-0.00428	-0.08468	7	0.00380	0.03847	0.00811	0.21091
-14	0.00373	0.09184	0.01365	0.14863	8	0.01085	0.04278	0.01802	0.42108
-13	-0.00521	0.10829	-0.01133	-0.10460	9	-0.00226	0.03667	0.00067	0.01838
-12	-0.00193	0.06315	-0.00478	-0.07563	10	0.00399	0.02544	0.00348	0.13673
-11	0.00634	0.04253	0.00302	0.07100	11	-0.00075	0.02674	0.00083	0.03111
-10	-0.00017	0.05710	0.01127	0.19744	12	-0.00553	0.02417	-0.00979	-0.40526
-9	-0.00867	0.04381	-0.01763	-0.40447	13	0.00405	0.02335	0.00763	0.32670
-8	0.00151	0.02224	0.00390	0.17534	14	-0.00154	0.02216	-0.00212	-0.09565
-7	0.00163	0.02178	0.00332	0.15262	15	-0.00217	0.01839	-0.00419	-0.22814
-6	0.00650	0.02451	0.01435	0.58529	16	-0.00103	0.02681	-0.00209	-0.07795
-5	-0.00248	0.02313	-0.00805	-0.34801	17	0.00390	0.03599	0.00836	0.23214
-4	-0.00377	0.02076	-0.00571	-0.27511	18	-0.00585	0.02608	-0.01271	-0.48633
-3	-0.00035	0.03274	-0.00296	-0.09033	19	0.00068	0.01731	0.00143	0.08289
-2	0.00125	0.02356	0.00494	0.20949	20	-0.00010	0.01569	-0.00026	-0.01630
-1	0.00403	0.03438	0.00879	0.25579	21	0.00477	0.03129	0.00154	0.04915
0	0.00534	0.02985	0.01165	0.39018					

Standard deviations of all these event firms and rival portfolios were calculated along with calculation of CAAR and values of t statistics were calculated later on by dividing CAARS by standard deviations. The calculated data is shown Table 1. Abnormal stock returns, standard deviation, cumulative abnormal returns, and cumulative average abnormal returns of 63 event firms have also been given in this table.. The data shows that the values of 'statistics on dividend announcements is significant having value of .3901.
In table 2 we have portrayed average abnormal returns of event firm about 21 days before and 21 days after. It indicates

Table 2 Positive and negative effect

AAR	BEFORE	AFTER
POSITIVE	11	10
NEGATIVE	10	11

that there are 10 negative values out of 21 days before and dividend announcement and 11 are positive. Negative amount should insignificant impact values and vice versa. There are 11 values that are negative after the event and 10 values are positive. Same configuration is view in the cumulative average abnormal returns. After the event there is negative value very first day followed by 2 days positive values which prove the negative response to dividend announcement.
We have found that out of 21 days before the announcement of dividend, t values are significant for 9 days with insignificant value of -1.74 on 21st days. Out of 21 days, t statistics value is insignificant for 13 days.

3. CONCLUSIONS

From the above discussion, we have concluded that at aggregate level the news surprises and number of news both are negatively related to stock market activity in Pakistan. This relationship is statistically significant in case of trading volume but insignificant in case of stock returns. We also found the day of the week patterns in these relationships. This relation (market activity and news) is also robust with news importance and above average news. Although in most of the cases our relation is significant, but this relation is weak. The analysis reveals the fact that in Karachi Stock Exchange public information does not play as important role in day-to-day variations in stock returns than the role played by private information (and non-informational reasons). We also noted an interesting point regarding day of the week pattern in market activity. From trading volume point of view Wednesdays are most prominent as trading activity is very brisk on this day while Friday is very sluggish day, which can be due to short span of market time and Friday prayer. From return point of view Monday is the best day in which high returns are recorded but Friday it is worst, which show losses. The qualitative testing has been demonstrated that after the announcement of dividend there is significant impact on the share price of firm. It is interpreted that results are reliable with a regular impact on the behavior of investor, they showed that want to receive the short run benefit like cash dividend. This conform the theory of "a bird in hand" not "two in bushes."

We can prove this scenario through another research study about reaction of American Telephone and Telegraph stock price relation to time series analyses for a time series of 43 regular dividends announcement has depicted significant impact on the average price of share positively before the dividend announcement and after the dividend announcement day was about 4 percent.

Some of the researchers are of the view that dividend policy is immaterial. It does not put forth impact on the shareholder's wealth. So, the firm's wealth can depend on the accumulation of earning for generating capital gain through investing the retained earnings in profitable projects. It, therefore,is said that payment of dividend is leakage of earnings.

4. Future Implications

As this study provides a detailed analysis of dividend announcement impact on share prices, it can be helpful for the investors and investment managers in understanding the behavior of market with regard to dividend announcement. This study can be further expanded in future in other areas like impact of merger/Acquisition, stock split, stock repurchase and their impact on share prices. There is a lot of scope of this study because stock market all over the world are fluctuating abnormally and the analysts are unable to understand the underlying cause of these fluctuations-whether they are due to fundamental changes in the financial indicators of the company or due to speculation.

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