AN IMPACT OF DIVIDEND DECISIONS ON SHARE PRICES OF THE COMPANY: A STUDY OF SELECTED PHARMACEUTICAL COMPANIES

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ABSTRACT
The objective of present study is to analyze the impact of dividend decisions on the average share prices of selected pharmaceutical companies. The study is totally based on secondary data. 10 pharmaceutical companies who have regularly paid dividend during the last five years has constituted the sample of the study. The data regarding the average share prices is collected for 30 days before and 30 days after the declaration of dividend. T-test for paired sample means is used for measuring the impact of dividend decision on the average share prices of the selected pharmaceutical companies. The result of the study indicates that the share prices of the companies are not affected by the dividend declaration. It means that the shareholders’ wealth is irrelevant to the dividend declaration.

Keywords: Dividend declaration, Share prices, Pharmaceutical companies

INTRODUCTION
The investors are always interested to invest in such securities which give them maximum return. The level of return is always attached with the degree of risk. Thus, the investor tries to trade-off between risk and return. Dividend attracts the investors to invest in shares. Dividend is the barometer of financial position, solvency of the business, management efficiency and overall performance of the firm. Management should take care of the expectations of the shareholders while formulating dividend policy. Dividend policy determines the proportion of earnings to be distributed among shareholders as dividend and the proportion of earnings to be reinvested in the business. Both return to shareholders and growth are necessary but they are conflicting to each other. If the company pays higher amount of dividend, then there is less amount available for reinvestment.

Dividend payment should be preferred if it results in the maximization of shareholders’ wealth. If not, reinvestment is the better option. There are various opinions regarding the relationship between dividend and shareholders’ wealth. There are some theories which explain that dividend declaration affects the market value of shares. While, other theories explain that dividend and shareholders’ wealth are independent to each other.

Indian Pharmaceutical Industry
Indian pharma industry has an important position in the global pharmaceuticals industry. The Indian pharmaceuticals market is the third-largest in terms of volume and thirteenth-largest in terms of value. It has highest number of USFDA plants outside the USA. It’s amongst the global leaders in providing quality generics to the world.

India accounts for 20% of global exports in generics. In FY16, India exported pharmaceutical products worth $16.89 billion, with the number expected to reach $40 billion by 2020. Pharma exports in India grew at 9.44% in FY16 and are expected to register double digit growth in FY17.
Indian pharmaceutical companies are now investing on research and development. Historically, they used to spend less than 4% on R&D but now they spend about 8% of their sales into research and development efforts."

Industry is gearing up for the next level of growth driven by shift towards specialty products, customer centricity, focus on improving quality, operational efficiency and productivity and selective mergers & acquisitions. Even though growth has slowed down recently in the event of GST and demonetization they believe it will be in the top 10 global markets by 2020.

REVIEW OF LITERATURE

Asamoah, G. (2010) examined whether there was significant increase in the company’s share prices to dividend declaration with reference to Ghana Stock Exchange. The event study methodology was applied to attain the research objective. Further, the Wilcoxon Matched-Pair Signed-Ranked Test was applied in testing the null hypothesis. The conclusion was that the Ghana Stock Exchange was not semi-strong efficient so in the conclusion that the it must address itself to three types of efficiency – allocation efficiency, operational efficiency and pricing efficiency.

Attah-Botchwey, E. (2014) tried to find out the impact of payment of dividend and its relevance on the share prices of selected listed companies on the Ghana Stock Exchange (GSE) and whether it helps shareholders to make an informed decision on either maintain or withdraw their investment and then reinvest in other companies. For this purpose, Cal bank, Eco Bank and AngloGold Ashanti were selected randomly out of the 36 companies which were listed on the Ghana Stock Exchange. Sixty respondents (shareholders) were selected randomly out of the total shareholders of the companies which were selected for the study. The primary source of data was collected through questionnaire and the secondary data collected from the internet, journals like the national tax journal, journal of risk finance, journal of finance and corporate finance. It was concluded that if the payment of dividend increase, prices of shares also increases. This indicates that prices of shares increase of firms with higher payment of dividend and shares prices decreases of firms with lower dividend payment.

Iqbal, N., Ahmad, N., Ullah, H. and Abbas, A. (2014) tried to find how dividend affects stock prices of the different banking sector with reference to Pakistan. For the study, secondary data was used, and three banks of Pakistan taken as sample. The study concluded that there is relevance between the dividend announcements and the stock prices.

Jakata, O. and Nyamugure, P. (2013) examined the effects of dividend decisions on the share prices. Period of the study was 2003 to 2011; objective of the study was to determine the effect of dividend on the stock prices. Statistical tools like Pearson s Correlation Coefficient, Linear Regression Analysis and p – values analysis used for the analysis of the data. The results showed that i) there is no relevance between dividend decisions and share price of a firm ii) there is no relevance between earnings per share and the stock price. At the end, the study concluded that dividend decisions do not affect stock price.

Joshi, A. and Mayur, M. (2017) examined the share price reactions of top 20 Public sector companies by market capitalization which were listed in Bombay Stock Exchange (BSE), covering 20 days of announcement (before 10 days to after 10 days) during the period 2013-2016. Event study methodology used for the study, data collected from the websites of BSE and Money control. The findings revealed that there was a significant difference on the prices of shares in before and after declaration of dividend of the selected companies. So, investors are advised to consider dividend payments of the companies to make better investment decisions.

Kumar, R. and Waheed, A. (2015) examines the determinants of dividend policy in GCC market based on sample firms in UAE market. An analysis was conducted to understand the dividend trends among different industry sectors in UAE market. The analysis of approximately 120 listed companies reveal that 80 per cent of the companies paid cash dividends during the three-year period 2011-2013. The study also examines the various theoretical attributes used in financial literature to understand the
determinants of dividend policy. The partial least squares structural equations modelling (PLS-SEM) was used to test the alternate explanations of corporate dividend pay-out policy in the gulf market. The study finds support for residual theory and pecking order argument of dividends. Investment policy influences dividend policy. The results support the theory that firms with high growth rate in income requires higher capital expenditure and establish lower dividend pay-out on account of costly external financing. Liquidity is an important determinant of dividend decision. Stability of dividend payments is not a critical factor considered by financial markets in the region.

Rani, U. (2008) attempts to explore the links between dividend decisions and share price behaviour in Indian context. A sample of 500 companies which are on BSE were taken for the period of 1996 to 2006. Panel data approach used to analyse the relationship between dividend-retention and stock price behaviour. The sample is taken from six industries namely food and beverage, electricity, textile, mining, non-metallic and service sector. The results were based on the fixed-effect model which indicate that dividend retention ratio plays a significant role in explaining variations in stock returns.

OBJECTIVES OF THE STUDY

The objectives of this research work can be summarized as follows:

1. To understand the dividend policy of the selected pharmaceutical companies.

2. To analyse the impact of dividend declaration on the average share prices of selected pharmaceutical companies.

RESEARCH DESIGN

Sources of Data

The present study is totally based on the secondary data and the data is collected from the official website of Bombay Stock Exchange www.bseindia.com. Various articles and research papers are also reviewed for the better understanding of the subject matter of the study.

Period of the Study

The study covers the period of one year starting from 1st April, 2016 to 31st March 2017. The data related to average share prices of selected pharmaceutical companies 30 days before and 30 days after declaring dividend are considered for the study.

Sample of the Study

10 pharmaceutical companies are selected as a sample for the present study. The pharmaceutical companies who are listed on Bombay Stock Exchange and who have declared the dividend regularly during the last 5 years (2012-13 to 2016-17) are selected as a sample of the study. The list of such companies are as follows:

1. Glaxo Smith Kline
2. Sanofi India Ltd.
3. Strides Arcolab Ltd.
4. Dr. Reddy’s Laboratories Ltd.
5. Novartis India Ltd.
6. Glenmark Pharma Ltd.
7. Lupin Ltd.
8. Cipla Ltd.
9. Jubilant Life Sciences Ltd.
Hypothesis Formulation:

$H_0$: There is no significant difference between the average share prices of selected pharmaceutical companies 30 days before and 30 days after declaring dividend.

$H_1$: There is a significant difference between the average share prices of selected pharmaceutical companies 30 days before and 30 days after declaring dividend.

Significance of the Study:
The result of the study is useful to following parties:

1. This study provides useful information to investors related to possible changes in share prices due to dividend declaration.
2. It also helps financial managers and financial advisors in formulating dividend policy.

Limitation of the Study
The limitations of the study are as follows:

1. As the study conducted only for 10 pharmaceutical companies, the generalization of results cannot be made for whole industry.
2. The present study is totally based on secondary data. So, the limitations of using secondary data are also present in the study.

Framework of Analysis
T-test: paired two sample for means is used to examine the impact of dividend declaration on the share prices of selected pharmaceutical companies.

Here, \( \text{Average Share Price} = \frac{\text{Opening Share Price} + \text{Closing Share Price}}{2} \)

THEORIES OF DIVIDEND GIVEN BY VARIOUS AUTHORS

There are mainly three well known theories of dividend policy which are described as below:

Modigliani and Miller Hypothesis of Dividend Irrelevance:
Franco Modigliani and Merton H. Miller have advocated that, the dividend policy of a firm is irrelevant, because it does not affect the value of the shareholders. It means that the value of the firm is independent of its dividend policy. Value of the firm is dependent on the firm’s earning capacity, which result from the investment policy of the company and not from the dividend policy of the company. It means that for the determination of the value of firm, dividend decision is not a useful tool.

Walter’s Model of Dividend Relevance
James E. Walter has given the model of dividend theory in 1963, which explains that for determination of value of shareholders, dividend decision is important determinant. Investment decision and dividend decision are interlinked with each other. According to Walter, investment decision and dividend decision cannot be separated. If the company pays dividend, then the shareholders reinvest the same, to get higher returns. This is known as opportunity cost or cost of capital for the firm. If the company does not pay out the dividends and retains the earnings in profitable opportunities to earn returns. Thus, the rate of return for the firm must at least be equal to cost of capital.
Gordon’s Model of Dividend Relevance

Myron J. Gordon has given the dividend relevance theory and explained that the dividend decision of the firm affects the share prices of firms. Investors are risk averse and believe that dividend incomes are certain instead of the incomes from further capital gains. Therefore, they assume that future capital gains are riskier. That’s why they prefer present dividend instead of future capital gains.

ANALYSIS USING T-TEST: PAIRED TWO SAMPLE MEANS

The table given below shows the average share prices of selected pharmaceutical companies before and after 30 days of dividend declaration.

<table>
<thead>
<tr>
<th>Companies</th>
<th>Before</th>
<th>After</th>
</tr>
</thead>
<tbody>
<tr>
<td>Glaxo Smith Kline</td>
<td>2494.47</td>
<td>2428.80</td>
</tr>
<tr>
<td>Sanofi India Ltd.</td>
<td>4565.67</td>
<td>4132.56</td>
</tr>
<tr>
<td>Strides Arcolab Ltd.</td>
<td>972.86</td>
<td>911.75</td>
</tr>
<tr>
<td>Dr. Reddy’s Laboratories Ltd.</td>
<td>2648.96</td>
<td>2291.46</td>
</tr>
<tr>
<td>Novartis India Ltd.</td>
<td>634.19</td>
<td>610.99</td>
</tr>
<tr>
<td>Glenmark Pharma Ltd.</td>
<td>614.75</td>
<td>611.25</td>
</tr>
<tr>
<td>Lupin Ltd.</td>
<td>1121.32</td>
<td>998.57</td>
</tr>
<tr>
<td>Cipla Ltd.</td>
<td>548.88</td>
<td>565.16</td>
</tr>
<tr>
<td>Jubilant Life Sciences Ltd.</td>
<td>253.65</td>
<td>216.65</td>
</tr>
<tr>
<td>Sun Pharmaceutical Industries Ltd.</td>
<td>485.44</td>
<td>527.03</td>
</tr>
</tbody>
</table>

By applying t-test the following results are obtained for the selected pharmaceutical companies:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Before</th>
<th>After</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>1434.02</td>
<td>1329.42</td>
</tr>
<tr>
<td>Variance</td>
<td>1900643.02</td>
<td>1530418.64</td>
</tr>
<tr>
<td>Observations</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>Hypothesized Mean Difference</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Df</td>
<td>9</td>
<td></td>
</tr>
<tr>
<td>t Stat</td>
<td>2.06</td>
<td></td>
</tr>
<tr>
<td>P(T&lt;=t) one-tail</td>
<td>0.03</td>
<td></td>
</tr>
<tr>
<td>t Critical one-tail</td>
<td>1.83</td>
<td></td>
</tr>
<tr>
<td>P(T&lt;=t) two-tail</td>
<td>0.07</td>
<td></td>
</tr>
<tr>
<td>t Critical two-tail</td>
<td>2.26</td>
<td></td>
</tr>
</tbody>
</table>
STATISTICAL ANALYSIS

1. Since the value of ‘t’ in the table at 5% level of significance and with degree of freedom n-1 = 9, is more than the calculated value in case of average share prices of the selected Pharmaceutical Companies declaring dividends, hence the H0 is significant and accepted.

2. Hence, we can say that there is no significance difference between the average share prices of selected 10 pharmaceutical companies before 30 days and after 30 days of declaring dividend.

3. It means that share prices of the selected pharmaceutical companies are independent from the firm’s dividend decision.

4. The result of the present study is supported by Modigliani and Miller Hypothesis of Dividend Irrelevance theory. According to this theory, the share prices of the firm is independent from its dividend decision.

5. The MM approach is based on the operation of arbitrage. It means if the company retains earnings, then the shareholders enjoy capital appreciation which is equal to the amount of retained earnings. If the company pays out the dividend, then the shareholders enjoy dividend which is equal to the value of capital appreciation. Thus, the dividend decision is irrelevant for the determination of shareholders’ wealth.

6. Two companies who have same amount and same type of risk, having same future prospective of earnings and same investment policies will have the same market price of the shares, irrespective of their dividend decisions.

CONCLUSION

The result of the study expresses that the dividend declaration does not affect the average share prices of the firm. It means whether the company pays the dividend or not, it doesn’t make any difference on the average share prices of the selected pharmaceutical companies. The result of the study is supported by the Modigliani and Miller Hypothesis of Dividend Irrelevance theory.

REFERENCES


