



Impact of Dividend Announcement on Stock Price: Empirical Evidence of Colombo Stock Exchange

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Abstract

Dividend deceleration is clearly important competent among the shareholders. With the dividend announcement investors treated with the dividend gain according to their investment. It has been identified that dividend deceleration has both signal in increase and decrease the share price. And also, reaction of share price depends on the market condition too. The present study is an attempt to study the price reaction of 161 dividend announcements by 19 companies during the period 2013 to 2017 among listed S & P 20 companies in CSE. The analysis had been developed using event study method. The study exposed the fact that stock prices do react to dividend announcements and dividend announcements made the difference between share price prior to the dividend announcement and share price after dividend announcement.

1. Introduction

The stock market is the place where the numbers of investors are making their investment decisions. As per the company performances and information are influencing on the stock price, the perception of the investors on the company share are also important. Based on the investors' perception on the stock market and individual shares are create the demand and supply for the individual shares. Mostly the company announcement, changes in director board, company acquisition or merging and financial statements disclosures are influencing on the stock price changes. And also, divided announcements are influencing on the stock price in relating to the dividend announcement date. Most of the existing theories and also the previous research studies explain that the dividend announcements are impact on the stock prices changes. The aim of this study to investigate the relationship among the dividend announcement and the share prices changes due to dividend announcement date.

1.1 Statement of the Research Problem

Accounting and financial information relating to the company is creating the changes in perception of investors regarding the investment decisions. As per the financial statements which provide the results of company operations and also the dividend announcement effect on the share prices in different ways in the capital market. Basically, the history of the divided explains the role of popularity in the dividend and the declaration and payment of dividend in the company effect the share price in timely. Therefore, the investors are much considerable in the dividend announcement made by the companies and its effect on the share price. Most common perception of the dividend discuss that the dividend announcing is positively impact on the share price. Therefore, the variables of dividend announcement and the share price should be analyzed to understand how the dividends are effect on the share price and the investor's perception.

1.2 Research Question

The main purpose of this research is to identify the relationship between share price changes in relating to the dividend announcements. To examine the share price changes along with the dividend announcements, following research question have been formed;

- What is the relationship between share price changes in relating to the dividend announcements?

1.3 Research Objective

The major objective of the study is to identify the share price reaction relating to the dividend announcements. The specific objective of the study is;

- To examine the effect of dividend announcements on efficiency of stock pricing with the empirical evidence from Colombo Stock Exchange

1.4 Significance of the Research

Using the results of the study helps to investors in their investment decision making align with the dividend announcements in equity capital market in Sri Lanka. The existing investors those who have experienced in dividend announcement can acquire the proper knowledge and practical situation of the dividend announcements and share price changes in the current market conditions. And also, the peoples who are interesting to invest in the equity capital market can have the better understanding on their investment decision in equity market in Sri Lanka.

2. Literature Review

Major objective of the shareholders is to maximize their wealth. In purposing of the wealth maximization, declaring the dividend is important to each shareholder. But, it is still unsolved that to confirm the dividend policy impact on the shareholder wealth maximization, (Suwanna 2012, p. 721). It is important to consider the short-term effect and the long-term effect of the dividend announcement. And also, managers must be concern with the dividend policy and its impact of stock risk. And also, managers can use the dividend policy in order to control the volatility of share price, Anwar et al (2015 p. 46).

Dividend announcement in an organization gives a positive signal to the shareholders. Share price react on the market information such as different market microstructure, tax regime and control environments, Gupta et al (2012, p.30). Stankeviciene & Akelaitis (2014, p. 542) explained that number of public announcements are impact in different manner with the share price.

Mehndiratta & Gupta (2010, p. 405) discussed that dividend announcements are impact on the share price and it will take a positive reaction when the expectation level of shareholders match with declared dividend. And also, if the shareholders expectation level does not match with declared dividend then the market reaction will in bear trend for it.

Gupta et al (2012, p.23, 24) discussed that some situation occurs in imperfect market condition between managers and the investors. Suwanna (2012, p. 723) conclude on the research that dividend announcements are significantly impact on the share price. Asamoah (2010, p.57) noted that price-efficient market leads to adjust risk of the investors and the price of the stocks are not changing rapidly and biased according to the new information relating to the share price.

Anwar et al (2015 p. 46) noted that the divided announcement are creates a best return for trading in short-term and investors can get the capital gain due to the price changes in share accordingly to the cash dividend.

Kadioglu (2015, p. 91) concluded on the research findings that dividend per share and the abnormal return have negative relationship after the dividend announcement. It explains due to the after the cash dividend announcement most of the investors are start to sell the shares to reduce their tax expenses. Therefore, the relationship between dividend per share and the abnormal return after divided announcement had shown as negative. Pathirawasam (2009, p.111) conclude that price reaction on dividend announcement is high in Sri Lanka than the other countries with the data analysis according to the period of 1998 to 2007.

3. Research Methodology

The Event Study Method proposed by Lonie et al (1996), Ghada (2015), Waweru & Otieno (2016), Pathirawasam (2009), Gupta et al (2012), Stankeviciene and Akelaitis (2014), Suwanna (2012) and Anwar et al (2012), are used to analyze the share price changes in the stock market with effect to the divided announcement date. The procedure for event studies is to investigate whether there are abnormal returns around the announcement date.

Daily abnormal returns for the security ‘i’ from 10 days before and 10 days after the dividend announcement (including announcement day) of the dividend increase has been computed as

$$AAR_{(i,t)} = R_{(i,t)} - E(R_{i,t})$$

Where,

AAB - Average abnormal return on security “i” for day “t”

R - Market price of the security “i” for day “t”

E (R) - Expected return of the security “i” for day “t”

Expected return of the stock computed with the 30 days before the divided announcement date with

$$\frac{1}{N} \sum_{i=1}^n AR$$

Where:

AR - Average return for 30 days before dividend announcement date

3.1 Operationalization of Variables

| Concept | Indicator | Measure | Reference |
|----------------------|---|---|---|
| Independent Variable | Share price before dividend announcement date | Average share price measure before dividend announcement date | Gupta <i>et al</i> (2012), Stankeviciene & Akelaitis (2014), Suwanna (2012), Anwar (2015), Yahyaee (2015), Mehndiratta & Gupta (2010), Chavali & Nusratunnisa (2013), Kadioglu <i>et al</i> (2015) |
| Dependent Variable | Share price after dividend announcement date | Average share price measure after dividend announcement date | Gupta <i>et al</i> (2012), Stankeviciene & Akelaitis (2014), Suwanna (2012), Anwar, S (2015), Yahyaee (2015), Mehndiratta & Gupta (2010), Chavali & Nusratunnisa (2013), Kadioglu <i>et al</i> (2015) |

3.2 Conceptual Framework

Dividend serves as a popular income source for the investors. Dividend will declare from the profit generated by the organization and it will make a strong perception among the investors to encourage increasing their investments. The study of the dividend announcements and share price changes has two main indicators with reflecting to the dividend announcement date. Share price before dividend announcement date indicates as the independent variable and share price after dividend announcement date indicate as the dependent variable. The model of the research can be explained as follows;

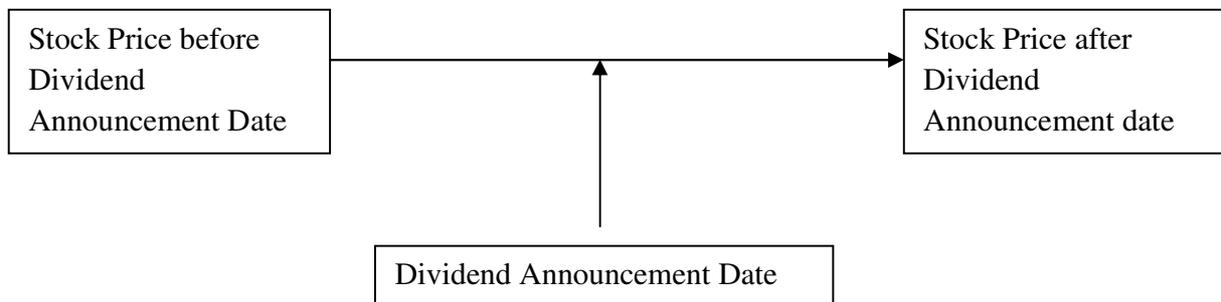


Figure 1.1 Conceptual Framework

3.3 Hypothesis

In order to find the relationship between dividend announcement and the share price, the following hypothesis is formed.

$$H_0: \mu_A = \mu_B$$

$$H_1: \mu_A \neq \mu_B$$

μ_A : Mean value of share prices after dividend announcement

μ_B : Mean value of share prices before dividend announcement

In the same manner the hypothesis we can explain the following way of consider;

H₀: There is no difference between share prices prior to the dividend announcement and after the dividend announcement

H₁: There is a difference between share prices prior to the dividend announcement and after the dividend announcement

3.4 Research Sample

There are 295 listed companies in Colombo Stock Exchange under 20 sectors. All listed companies which are registered in Colombo Stock Exchange consider as the proposed population of the research study. Sample of the population will be selected S & P 20 companies which has been announced the dividend within 2013 – 2017.

3.5 Method of Data Collection and Evaluation

Data will be collected before 10 days from the date of dividend announcement and 10 days after the dividend announcement with effect to 30 days average return of before dividend announcement date.

The collected data was analyzed by using the SPSS software (version 16.0) and paired sample t-test will be used to interpret the significance and the mean deference of the changes in share price based on the dividend announcement.

4. Data Analysis

Number of dividend announcements of companies is depending on their managerial decision making. According to the sample of 20 S & P companies in Colombo Stock Exchange, Table 4.1 illustrates number of dividend announcements made by the individual companies during 2013 to 2017 including the cash dividend and scrip dividend. Company code LOLC.N0000 has not made any dividend announcement during the period of 2013 to 2017.

Table 4. 1 Frequency of Dividend Announcements

| Serial no | Company Code | Number of announcements made during 2013 to 2017 | Serial no | Company Code | Number of announcements made during 2013 to 2017 |
|-----------|--------------|--|-----------|--------------|--|
| 01 | RICH.N0000 | 07 | 11 | LLUB.N0000 | 20 |
| 02 | DIAL.N0000 | 05 | 12 | HHL.N0000 | 10 |
| 03 | PLC.N0000 | 10 | 13 | LOLC.N0000 | 0 |
| 04 | AEL.N0000 | 12 | 14 | DFCC.N0000 | 05 |
| 05 | VONE.N0000 | 05 | 15 | NDB.N0000 | 11 |
| 06 | SHL.N0000 | 04 | 16 | COMB.N0000 | 14 |
| 07 | TKYO.N0000 | 05 | 17 | JKH.N0000 | 14 |
| 08 | TJL.N0000 | 10 | 18 | HNB.N0000 | 10 |
| 09 | SPEN.N0000 | 06 | 19 | SAMP.N0000 | 07 |

| | | | | | |
|-------|------------|----|----|------------|-----|
| 10 | MELS.N0000 | 01 | 20 | CINS.N0000 | 05 |
| Total | | | | | 161 |

Table 4.2 shows the average share price for S & P Companies involved in the study sample before and after the event. (10 days before and 10 days after the financial statement disclosure for five years' average data). Average abnormal returns shown in the table 4.2 is the average of 19 S & P companies. Stock price reaction of individual company has been calculated according to the dividend announcement date and average abnormal returns of individual companies are shown in the appendix.

Table 4. 2 Average Abnormal Return

| Serial | Days before \ after | Average Abnormal Return |
|--------|---------------------|-------------------------|
| 1 | -10 | -0.22837 |
| 2 | -9 | -0.07926 |
| 3 | -8 | 0.748163 |
| 4 | -7 | 0.878101 |
| 5 | -6 | 0.606922 |
| 6 | -5 | 1.454001 |
| 7 | -4 | 2.090159 |
| 8 | -3 | 2.32215 |
| 9 | -2 | 0.086268 |
| 10 | -1 | 2.433697 |
| 11 | 0 | 2.510676 |
| 12 | 1 | 3.175703 |
| 13 | 2 | 3.092581 |
| 14 | 3 | 2.038597 |
| 15 | 4 | 2.927699 |
| 16 | 5 | 2.383909 |
| 17 | 6 | 1.481519 |
| 18 | 7 | 0.859804 |
| 19 | 8 | 0.790894 |
| 20 | 9 | 2.580346 |
| 21 | 10 | 2.539428 |

The immediate day following the dividend announcement had shown the increase of abnormal return. Anwar et al (2015 p. 46) discussed that in short-term of dividend

announcement made the best return for trading. Further the share price reaction on the shown in the figure 4.1.

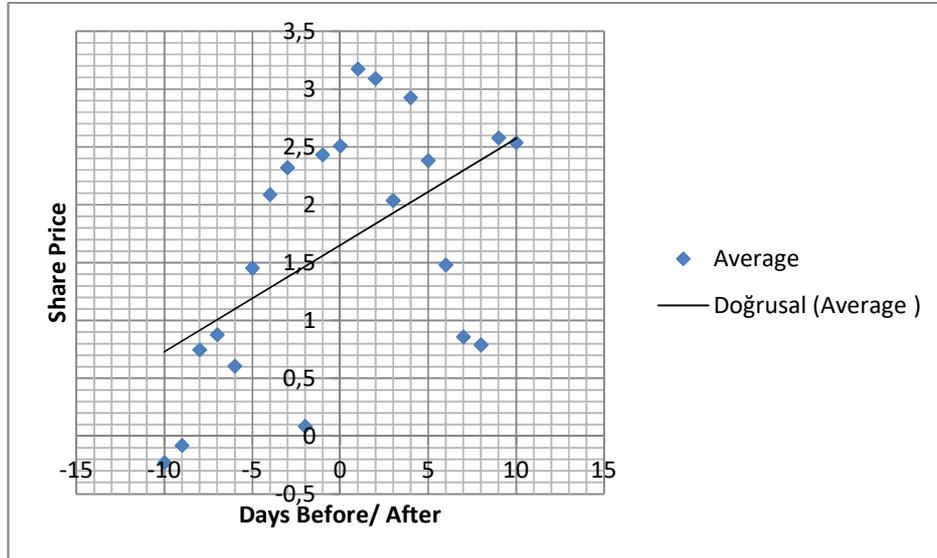


Figure 4.1 Total Average Abnormal Return

Table 4. 3 Parried Sample t-test

| | | Paired Samples Statistics | | | | | | | |
|------------|----------------------------------|---------------------------|----------------|-----------------|---|------------|--------------|-----------------|-------------|
| | | Mean | N | Std. Deviation | Std. Error Mean | | | | |
| Pair 1 | Pre-Announcement | 1.03118300 | 10 | .996092534 | .314992117 | | | | |
| | Post Announcement | 2.18704800 | 10 | .875229106 | .276771745 | | | | |
| | | Paired Samples Test | | | | | | | |
| | | Paired Differences | | | | | | | |
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | t | Sig. (2-tailed) | |
| | | | | | Lower | Upper | | | |
| Pair Pre-1 | Announcement - Post Announcement | 1.155865003 | 1.219114118 | .385517734 | 2.027966707 | .283763300 | 2.998 | 9 | .015 |

Mean difference between share price before and after the dividend announcement is -1.155565003. Since the p value is 0.015, there was a significant average difference between share price before and after the dividend announcements. ($t_9 = -2.998$, $p < 0.05$). On

average share price before the dividend announcement were 1.155565003 lower than the share price after the dividend announcement. (95% CI [-2.027966707, -0.283763300]).

Table 4.4 Decision Table

| H0 | H1 | P value | Decision | Conclusion |
|-----------------|--------------------|---------|-----------|---|
| $\mu_A = \mu_B$ | $\mu_A \neq \mu_B$ | 0.015 | Reject H0 | There is a significant difference between share price before and after the dividend announcement. |

5. Conclusion

Dividend policy is an important component for share holders. Most of the shareholders are considered in both capital gain and divided gain on equity shares. According to the data analysis, share price reaction on the dividend accountments discussed that, as the p value from the paired sample t-test ($p = 0.015$) less than 0.05, there is sufficient evidence to reject the null hypothesis. Therefore, it can be concluded that there is a difference between share price prior to the dividend announcement and share price after dividend announcement. Chavali and Nusratunnisa (2013, p. 08) noted that there are some indication that dividend announcements do have an impact on share price and specially share price change the date and three postdate on dividend announcement. Further table 4.3 and figure 4.1 explain the higher mean value of share price in post announcement. Therefore, it concludes that after dividend announcement share price tend to increase. On the other way, other market information and market conditions also can be influence on the share price changes. Therefore, it should be concerne the other relevance factors which may be able to influence on the share price changes other than the dividend announcement information. Ghada (2015 p. 133) discussed that share price changes in stock due to the dividend announcement as well as the other factors which may affecting investors' behavior such as economic and political.

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Appendix

S & P 20 Companies Average Abnormal Return

| | RICH. N000 0 | DIAL.N 0000 | PLC.N 0000 | AEL.N 0000 | VONE.N 0000 | SHL.N 0000 | TKYO.N 0000 | TJL.NO 000 | SPEN.N 0000 | MELS.N 0000 |
|-----|--------------------|----------------|---------------|---------------|----------------|---------------|----------------|---------------|----------------|----------------|
| -10 | -0.040 | 0.115 | 0.118 | 0.115 | 0.329 | -0.049 | -0.465 | 0.101 | 0.366 | -0.083 |
| -9 | 0.003 | 0.035 | 0.208 | 0.040 | 0.109 | -0.074 | -0.765 | 0.301 | 1.199 | -1.083 |
| -8 | 0.060 | 0.035 | 0.218 | -0.035 | -0.151 | 0.051 | -0.325 | 0.331 | 1.883 | -0.083 |
| -7 | 0.003 | 0.075 | 0.258 | 0.015 | -0.171 | 0.151 | -0.125 | 0.391 | 1.233 | -0.083 |
| -6 | 0.017 | 0.135 | 0.238 | -0.002 | -0.171 | 0.251 | -0.325 | 0.231 | 1.249 | -0.083 |
| -5 | 0.017 | 0.215 | 0.198 | 0.240 | -0.231 | 0.151 | -0.425 | 0.221 | 1.266 | 0.017 |
| -4 | 0.060 | 0.095 | 0.298 | 0.432 | -0.191 | 0.201 | -0.325 | 0.171 | 1.966 | -1.583 |
| -3 | 0.046 | 0.135 | 0.238 | 0.257 | -0.311 | 0.151 | -0.405 | 0.241 | 2.583 | -1.783 |
| -2 | -0.026 | 0.095 | 0.308 | 0.340 | -0.071 | 0.176 | -0.245 | 0.181 | 3.249 | -0.083 |
| -1 | 0.046 | 0.195 | 0.308 | 0.565 | -0.171 | 0.176 | 0.495 | 0.191 | 4.516 | -0.383 |
| 0 | 0.031 | -1.765 | 0.318 | 0.807 | -0.191 | 0.126 | 0.515 | 0.271 | 4.883 | -1.483 |
| 1 | 0.231 | 0.175 | 0.468 | 0.957 | -0.031 | 0.226 | 0.795 | 0.521 | 4.649 | -2.383 |
| 2 | 0.217 | 0.235 | 0.468 | 1.248 | -0.091 | 0.326 | 1.275 | 0.491 | 4.566 | -3.183 |
| 3 | 0.246 | 0.215 | 0.438 | 1.265 | -0.031 | 0.276 | 1.435 | 0.381 | 4.633 | -1.783 |
| 4 | 0.246 | 0.215 | 0.368 | 1.323 | -0.111 | 0.401 | 1.015 | 0.451 | 4.133 | -3.383 |
| 5 | 0.246 | 0.175 | 0.358 | 1.273 | -0.051 | 0.426 | 1.015 | 0.391 | 4.183 | -2.983 |
| 6 | 0.231 | 0.175 | 0.438 | 1.157 | -0.051 | 0.251 | 1.235 | 0.311 | 3.316 | -2.883 |
| 7 | -0.083 | 0.215 | 0.088 | 0.740 | -0.411 | 0.001 | 1.235 | -0.049 | 3.516 | -3.283 |
| 8 | -0.083 | 0.215 | 0.078 | 0.790 | -0.411 | -0.224 | 1.295 | -0.019 | 3.433 | -3.183 |
| 9 | -0.069 | 0.155 | 0.038 | 0.590 | -0.451 | -0.049 | 1.115 | 0.151 | 3.299 | -3.983 |
| 10 | 0.031 | 0.155 | -0.012 | 0.332 | -0.431 | -0.124 | 0.935 | 0.091 | 3.799 | -4.083 |

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| | LLUB. N0000 | HHL.NO 000 | DFCC.NO 000 | NDB.NO 000 | COMB.NO 000 | JKH.NO 000 | HNB.NO 000 | SAMP.NO 000 | CINS.NO 000 |
|------------|------------------------|-----------------------|------------------------|-----------------------|------------------------|-----------------------|-----------------------|------------------------|------------------------|
| -10 | -1.373 | 1.672 | 3.035 | 0.365 | 0.427 | -1.727 | -1.065 | 0.400 | -6.579 |
| -9 | -0.653 | 1.802 | 3.895 | 1.483 | -0.773 | -1.591 | -0.865 | 1.642 | -6.419 |
| -8 | 0.767 | 1.962 | 3.375 | 0.620 | -0.580 | -1.427 | 0.795 | 1.900 | 4.821 |
| -7 | 0.367 | 2.382 | 3.955 | -0.226 | -0.323 | -1.877 | 2.125 | 2.114 | 6.421 |
| -6 | 0.202 | 2.172 | 3.255 | -0.880 | -0.309 | -2.420 | 2.765 | 5.285 | -0.079 |
| -5 | 0.307 | 2.382 | 2.615 | 0.165 | -0.030 | -1.413 | 2.265 | 5.185 | 14.481 |
| -4 | -0.453 | 2.742 | 3.055 | 1.783 | 0.220 | -0.948 | 1.645 | 6.085 | 24.461 |
| -3 | -0.118 | 3.342 | 3.635 | 1.329 | -0.266 | -0.677 | 0.985 | 6.000 | 28.741 |
| -2 | -0.618 | 2.092 | 3.555 | 2.211 | 0.141 | 0.037 | 1.285 | 5.671 | -16.659 |
| -1 | -0.428 | 2.322 | 4.795 | 3.002 | 0.527 | -0.077 | 1.605 | 5.957 | 22.601 |
| 0 | -0.016 | 2.729 | 5.215 | 3.311 | 0.777 | -0.884 | 1.365 | 9.014 | 22.681 |
| 1 | -5.558 | 1.912 | 5.035 | 4.756 | 1.684 | -1.091 | 0.435 | 8.557 | 39.001 |
| 2 | -4.688 | 2.402 | 5.955 | 4.147 | 1.934 | -1.484 | 0.175 | 8.485 | 36.281 |
| 3 | -4.553 | 2.312 | 5.795 | 3.902 | 1.627 | -1.398 | -0.225 | 8.100 | 16.101 |
| 4 | -3.933 | 2.482 | 5.575 | 4.220 | 1.934 | -1.020 | -0.155 | 8.585 | 33.281 |
| 5 | -3.333 | 3.312 | 5.115 | 2.747 | 1.799 | -1.077 | 0.445 | 7.314 | 23.941 |
| 6 | -2.888 | 1.712 | 3.915 | 2.211 | 1.634 | -0.941 | 0.595 | 8.371 | 9.361 |
| 7 | -6.023 | 1.872 | 3.215 | -1.580 | 1.320 | -2.084 | 0.485 | 9.642 | 7.521 |
| 8 | -6.838 | 2.022 | 1.575 | -2.835 | 0.613 | -2.520 | 0.545 | 10.114 | 10.461 |
| 9 | -7.308 | 1.622 | 1.235 | -3.471 | 0.441 | -3.348 | 0.585 | 10.414 | 48.061 |
| 10 | -7.893 | 1.202 | 1.915 | -2.480 | 0.820 | -3.148 | 0.595 | 7.685 | 48.861 |