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EFFECT OF DIVIDEND POLICY ON STOCK MARKET PERFORMANCE OF LISTED DEPOSIT MONEY BANKS IN NIGERIA

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Abstract

The study investigated with the effect of dividend policy on stock market performance of listed deposit money banks in Nigeria. The study employed an ex-post facto research design. The research population comprises of twelve commercial banks listed on the Nigerian Exchange Group's trading platform as of December 31, 2022. The timeframe from 2013 to 2022, covering the financial years of the ten companies, was selected as the designated period for the research's focus. The data for this study are gotten from annual reports of the selected banks. The results indicate that DPS is significantly associated with MPS, demonstrating a positive relationship. Similarly, DPO and RER were found to have significant positive effects on MPS, suggesting that higher dividend payouts and retained earnings ratios contribute to better stock market performance. Bank size (BS), used as a control variable, also showed a significantly positive effect on MPS, indicating that larger banks tend to perform better in the stock market. However, the study found that dividend yield (DY) did not show any significant relationship with MPS. This suggests that while other dividend policy variables play a crucial role in influencing stock market performance, the dividend yield alone does not have a direct impact on the market price of shares for the listed commercial banks in Nigeria. The study recommended that the higher the profitability and operating cash flow of a firm, the higher the dividend payout ratio, leading to higher stock prices. Management should focus on enhancing the company's profitability and operating cash flow. This can be achieved through strategic investments, cost optimization, and efficient operations. By improving these financial metrics, the company can afford to increase its dividend payout ratio.

Introduction

Corporate dividend decisions are pivotal in managerial strategy and often form the cornerstone of financial management choices. These decisions encompass determining whether earnings should be distributed to shareholders or retained internally. Therefore, the interplay between dividend payout and retained earnings defines a firm's dividend policy. According to Al-Malkawi et al. (2010), dividend policy refers to the framework management uses to make dividend payout decisions. This policy also governs how dividends are calculated and when they are disbursed, serving as a reflection of a firm's commitment to regularly reward shareholders. While companies are not obligated to distribute dividends, the consistent payment of dividends remains crucial to managers. Managers recognize that such payments are vital for meeting shareholder expectations, and studies have shown that increases in dividends can positively influence share prices and, consequently, firm value. Moreover, Nancy and Sahi (2018), emphasizes that corporate dividend decisions significantly impact other corporate strategies, including investment, financing, and shareholder wealth.

Financial performance serves as a common ground for all stakeholders of a company-management, shareholders, government, potential investors, and regulators. These stakeholders are keenly interested in the company's liquidity position, which plays a critical role in achieving higher financial performance and consequently higher dividend payments. Given the interconnected nature of these variables, effective liquidity management is expected to enhance financial performance, thereby prompting increased dividend payouts by companies.

The relationship between dividends and financial performance is crucial in today's business environment, particularly in determining shareholder payouts. Dividend policy remains a contentious issue in corporate finance, with financial economists extensively modeling and analyzing its impact on companies and stock prices, as observed in Nigeria (Amidu, 2017). Dividend policy refers to the rules and guidelines a company employs to decide whether and how much to distribute to shareholders. Unlike interest on debt, dividends require approval from the company's directors before each payment (Scott, 2013). The dividend policy dictates the allocation of earnings between distribution to shareholders and retention within the company. It is significant because retained earnings are a primary and cost-effective internal source of financing, while dividends provide a desirable return on investment to shareholders.

Black (2006) referred to dividends as a ‘puzzle,’ a question that remains unanswered to this day. Investors generally seek returns on their investments through dividends paid by the firms in which they invest. Therefore, stock returns are of great interest to investors. Research has shown that dividend announcements affect the stock returns of the announcing firm. This is despite Miller and Modigliani's (1961) explanation that the value of the firm is unaffected by dividend policy in a world without taxes. In an efficient market, security prices reflect all publicly available information, eliminating any opportunity to make excess profits from this information because it is already captured in market prices (Fama, 2000).

Despite extensive research on the impact of dividend policy in different contexts, the relationship between dividend policy and stock market performance of commercial banks in Nigeria remains underexplored and inconclusive. Some studies suggest that a stable or growing dividend payout fosters investor confidence, potentially driving up stock prices and increasing market capitalization. Others argue that high dividend payments may reduce funds available for reinvestment, thereby limiting future growth prospects and negatively impacting stock market performance. The commercial banking sector in Nigeria faces additional challenges, such as fluctuating economic conditions, regulatory changes, and varying levels of investor trust. These factors may interact with dividend policy to produce unique effects on stock market performance. Hence, it becomes imperative to investigate how dividend policy influences the stock market performance of listed commercial banks in Nigeria, particularly in a dynamic and volatile economic environment.

Another challenge is that cash dividends from earnings mean giving shareholders a reward from something they already own in the company, which is offset by a decline in stock value. The conflicting interests of shareholders regarding dividend policy cannot be overemphasized; rational shareholders consistently demand higher dividends regardless of the firm's investment decisions. Finance managers face a dilemma in harmonizing dividend and investment decisions since both are crucial to the company's worth and the growth of stakeholder value. The Nigerian All-Share Index has exhibited significant volatility over the past decade (2012-2021), with a notable low of 20,669.38 in April 2020 (Nigerian Exchange, 2022).

The central problem of this research is to assess whether dividend policy significantly affects the stock market performance of listed commercial banks in Nigeria and to determine whether adopting a particular dividend strategy (high dividends, low dividends, or no dividends) is more beneficial for enhancing stock market performance in the Nigerian banking sector. This study aims to provide empirical evidence that will inform bank managers, investors, and policymakers on optimal dividend strategies in order to promote bank profitability and investor satisfaction.

Objectives of the Study

The main objective of the study is to examine the effect of dividend policy on stock market performance of listed commercial banks in Nigeria. Other specific objectives are as follows:

i. To examine the effect of dividend pershare on stock market performance of listed commercial banks in Nigeria.
ii. To examine the effect of dividend payout on stock market performance of listed commercial banks in Nigeria.
iii. To examine the effect of retained earnings ratio on stock market performance of listed commercial banks in Nigeria.
iv. To examine the effect of dividend yield on stock market performance of listed commercial banks in Nigeria.

Research Hypotheses

The following null hypotheses were formulated:

$H0_1$ Dividend per share has no significant effect on the stock market performance of listed commercial banks in Nigeria.

$H0_2$ Dividend payout has no significant effect on the stock market performance of listed commercial banks in Nigeria.

$H0_3$ Retained earnings ratio has no significant effect on the stock market performance of listed commercial banks in Nigeria.

$H0_4$ Dividend yield has no significant effect on the stock market performance of listed commercial banks in Nigeria.

Literature Review

Market Share Price

The value of equity shares listed on the NGX daily is known as the market price per share (Olowe, 2017). This value represents the price per share of any entity at the end of each trading day. One of the most important indicators for investors when deciding whether to invest in a particular share is the share price (Gill et al., 2012). Unlike being constant, stock prices fluctuate daily in the market. The share price is the simplest to ascertain as it represents the price of a stock in the active market or the closing price if the market is closed. At the end of each trading day, supply and demand factors determine the market price of shares.

Dividend Policy

According to Ahmad et al. (2019) dividend policy is a crucial aspect of corporate financial management, balancing the immediate needs of shareholders with the long-term strategic goals of the company. By

carefully crafting and adhering to a dividend policy, financial managers can support the company's growth while ensuring shareholder satisfaction and market stability. Brealey and Myers (1996) assert that dividend decisions are frequently influenced by other financial and investment choices. Some businesses maintain low dividend payout rates due to management's future expectations regarding the company's value and the need to retain earnings for potential development and expansion. According to Harley and Duro (2017), a dividend is the distribution of past or present earnings among various equity investors according to their holding structure.

Dividend Price Ratio

The dividend price ratio, also known as the dividend yield ratio, is calculated by dividing the dividend per share by the share's price. It represents the annual dividend payments of a company as a percentage of its market value. Gordon (1962) developed a model to forecast the discount rate and dividend growth, suggesting that high dividends would be less sensitive to the discount rate and exhibit less price volatility. While the dividend price ratio can forecast future share price returns, it is not a reliable predictor of future dividend growth. Despite this, some market participants and scholars argue that the dividend price ratio is an effective indicator of future dividend increases, sparking a debate over its capacity to estimate future share returns.

Theoretical Review

Dividend Relevance: The Gordon's Model

Myron Gordon developed a widely recognized model that explicitly links the market value of a firm to its dividend policy. Gordon's model is built upon several key assumptions to illustrate how dividend decisions impact firm valuation:

(a) **All-Equity Firm**: The firm is assumed to have no debt; it operates entirely through equity financing.
(b) **No External Financing**: External financing is unavailable, meaning all expansion and investment are funded internally through retained earnings. This setup integrates dividend and investment policies similarly to Walter's model.
(c) **Constant Return**: The internal rate of return *(r)* of the firm is constant over time. This assumption simplifies the analysis but disregards the potential diminishing marginal efficiency of investment.
(d) **Constant Cost of Capital**: The discount rate *(k)* used to calculate the present value of future dividends remains constant. This assumption overlooks the impact of changes in the firm's risk profile on its cost of capital.
(e) **Perpetual Earnings**: The firm and its stream of earnings are perpetual, ensuring that the model's conclusions apply over an indefinite time horizon.
(f) **No Taxes**: Corporate taxes are assumed not to exist, simplifying the calculation of dividends and their impact on shareholder wealth.
(g) **Constant Retention**: Once established, the retention ratio *(b)* is assumed to remain constant. Consequently, the growth rate of earnings *($g = br$)* is also constant indefinitely.
(h) **Cost of Capital Greater than Growth Rate**: The discount rate *(k)* is greater than the growth rate *($g = br$)*. This condition ensures that meaningful values for share prices can be derived from the model.

Gordon's formula for determining the present value of the firm's share price \(P_0 \) incorporates these assumptions:

$$P0 = DIVt/(1+k)^t/(1+k)^n/(1+k) - 1$$

Where:

- *P0* = Present value of the share price (market value of the firm)
- *DIVt* = Dividend per share in period t
- *k* = Cost of capital (discount rate)
- *n* = Number of periods (years)

In this formula, represents the discounted value of all future dividends, adjusted for the time value of money using the firm's cost of capital *k*. The model illustrates how dividend policy influences shareholder wealth by considering the trade-off between current dividend payments and future growth opportunities funded by retained earnings.

Empirical Review

Ugwu et al. (2020) conducted a study using multiple regression analysis to investigate the impact of dividend policy on corporate financial performance among consumer goods companies listed on the Nigerian Exchange (NGX). Their study collected data randomly from ten companies operating in the consumer goods sector between 2015 and 2019. Dividend payout ratio (DPR) and dividend per share (DPS) were utilized as proxies for dividend policy, while return on equity (ROE) served as a measure of corporate financial performance. The findings indicated a positive relationship between the proxies for dividend policy and ROE. Specifically, DPS showed a statistically significant positive effect on corporate performance, whereas DPR and EPS did not demonstrate a statistically significant effect.

Ahmad et al. (2018) conducted a study to explore the relationship between stock price volatility and dividend policy among companies listed on the Amman Stock Exchange. They gathered data from 228 firms spanning the years 2010 to 2016, accumulating a total of 1596 observations per firm year. The study employed descriptive statistics, Pearson Correlation, and Panel GMM estimation techniques to analyze the data. Their findings indicated a strong negative correlation between stock price volatility and both dividend yield and payout.

Shahid et al. (2020) conducted an empirical investigation into the impact of dividend policy on stock price volatility within Pakistan's auto industry. They analyzed data from seventeen vehicle companies listed on the Pakistan Stock Exchange from 2005 to 2016. Their findings, derived from empirical analyses, suggested that both dividend yield and payout ratio had a slight negative effect on share prices, although the impact was not statistically significant.

Simajuntak (2022) extended the exploration by investigating the combined impact of macroeconomic factors and dividend policies on stock prices. The study, focused on manufacturing firms in the basic and chemical industries listed on the Indonesia Stock Exchange from 2016 to 2020, measured macroeconomics through inflation, interest rates, and exchange rates, while dividend policy was assessed using the dividend payout ratio (DPR). Using regression with panel data, the research concluded that stock prices were significantly influenced by exchange rates but showed no significant impact from DPR, inflation, or interest rates.

Methodology

An ex-post facto research design is adopted for the study. The research population comprises the twelve commercial banks listed on the Nigerian Exchange Group's trading platform as of December 31, 2022. A comprehensive approach, also referred to as purposive sampling, was employed to selected ten commercial banks listed on the Nigeria Exchange Group. The timeframe from 2013 to 2022, covering the financial years of the ten companies, was selected as the designated period for the research's focus.

Model Specification

The model specification for study is given as:

$MPSit = \alpha 0 + \beta_1 DPSit + \beta_2 DPOit + \beta_3 RERit + \beta_4 DYit + \beta_5 BSit + Єit.$

Where,

α = shows the unknown intercept for every entity (n entity-specific intercepts)

β = coefficient of variable

MPS = Market price per share

DPS = Dividend per share

DPR = Dividend payout ratio

RER = Return earnings ratio

DY = Dividend yield

BS = Bank size

Є = Error term in the equation

i = company

t = time.

Analysis and Interpretation

Descriptive Statistics

Table 1: Summary of descriptive Statistics

Variable	Obs.	Mean	Std. Dev.	Minimum	Maximum
MPS	100	130.8490	78.536	10.6	328.60
DPS	100	0.5797	0.5653	0	1.95
DPO	100	0.3323	0.3920	0	1.75
RER	100	1.9652	3.9506	0	36.78
DY	100	6.4462	4.3396	0	22.15
BS	100	9.1977	0.3966	7.95	9.84

Source: Stata, 2024

Table 1 presents the descriptive statistics of the variables included in the model, generated using Stata version 14. These statistics encompass the mean, standard deviation, minimum, and maximum values for each variable. The mean value for MPS in Nigerian banks is 130.849, with a minimum value of 10.6 and a maximum value of 328.6, indicating a moderate range of variation in the market share prices of the listed commercial banks in Nigeria. The mean value for DPS is 0.5797, with a minimum of 0 and a maximum of 1.95, and a standard deviation of 0.5656. This suggests that while some banks did not pay any dividends, others paid up to 1.95 per share, with a reasonable level of variability. The mean DPO is 0.3323, with a minimum value of 0 and a maximum of 1.75, and a standard deviation of 0.3920. This indicates that some banks did not distribute any dividends, while others distributed up to 1.75 times their earnings, with a notable degree of variability. The mean value for RER is 1.9652, with a minimum of 0 and a maximum of 36.78, and a standard deviation of 3.9506. This wide range and high standard deviation indicate significant differences in the proportion of earnings retained by the banks. The mean DY is 6.4462, with a minimum of 0 and a maximum of 22.15, and a standard deviation of 4.3396. This suggests considerable variation in the dividend yield among the banks, from no yield to a high of 22.15. Serving as the control variable, the mean value for BS is 9.1977, with a minimum of 7.9521 and a maximum of 9.8402. This indicates limited disparity in the sizes and strengths of the listed commercial banks in Nigeria.

Correlation Analysis

Table 2: Summary of Pearson Correlation Matrix

	MPS	DPS	DPO	RER	DY	BS
MPS	1.0000					
DPS	0.7599	1.0000				
DPO	0.3236	0.5643	1.0000			
RER	0.0588	0.2355	0.0329	1.0000		
DY	0.0795	0.1730	0.0866	0.0016	1.0000	
BS	0.3704	0.3264	0.1669	0.0458	0.1410	1.0000

Source: Stata, 2024

Table 2 presents the Pearson correlation matrix, which delineates the relationships between the independent variables—Dividend Per Share (DPS), Dividend Payout Ratio (DPO), Retained Earnings Ratio (RER), and Dividend Yield (DY)—and the control variable, Bank Size (BS), with the market price of shares (MPS) of commercial banks listed on the Nigerian Exchange Group.

From Table 2, it is evident that there are no correlations among the variables in the model at the 1% and 5% significance levels. The correlation observed between MPS and DPS, with a correlation coefficient of 0.7599, indicates a strong positive relationship. Additionally, MPS shows a moderate positive correlation with DPO at 0.3236, a weak correlation with RER at 0.0588, another weak correlation with DY at 0.08, and a moderate correlation with BS at 0.3704.

DPS also displays various correlations with the other variables: a moderate correlation with DPO at 0.5643, a weak correlation with RER at 0.2355, another weak correlation with DY at 0.1730, and a moderate correlation with BS at 0.3264.

Moreover, DPO correlates weakly with RER at 0.0329, DY at 0.0866, and BS at 0.1669. RER has an extremely weak correlation with DY at 0.0016 and a weak correlation with BS at 0.0458. Finally, DY has a weak correlation with BS at 0.1410.

These correlations provide insight into the interrelationships among the variables in the model, highlighting the varying degrees of association between the independent and control variables with the market price of shares of commercial banks listed on the Nigerian Exchange Group. This information is crucial for understanding the dynamics at play and for making informed decisions based on these relationships.

Table 4.3 Regression results

Variables	Coefficient	t	P>|t|
DPS	119.4232	10.43	0.000
DPO	-34.68479	-2.27	0.026
RER	-2.864767	-2.22	0.029
DY	-1.324359	-1.15	0.254
BS	26.83039	2.04	0.044
Number of obs.	100		
F (5, 94)	32.48		
Prob > F	0.0000		
R-squared	0.6334		
Adj. R-squared	0.6138		
Root MSE	48.803		

Source: Stata, 2024

The model using linear regression analysis, several indicators were utilized. Among these is the R-Squared (R^2) coefficient, which assesses the robustness of the regression equation. Also known as the coefficient of determination, R^2 reveals the extent to which the dependent variable is explained by the model's independent variables. In this study, R^2 indicates the proportion of variance in the dependent variable, market price of shares (MPS), that is explained by the collective influence of the independent variables: dividend per share (DPS), dividend payout ratio (DPO), retained earnings ratio (RER), and dividend yield (DY).

An R^2 value of 1 implies a perfect linear relationship between the dependent and independent variables, while an R^2 value of 0 indicates no linear relationship. Thus, the R^2 value represents the degree of variance in the dependent variable (stock market performance, measured using MPS) that is accounted for by the model, which includes DPS, DPO, RER, and DY.

As shown by the outcomes in Table 4.3, the R^2 value for the model is 0.6334. This means that the model explains 63.34% of the variance in stock market performance, as measured by MPS, which is considered an acceptable result. STATA (version 14) provides an adjusted R^2 value in the output to account for small sample sizes, as the R^2 value can be an optimistic overestimation of the true population value (Tabachnick & Fidell, 2007). The R^2 value of 0.6334 indicates that 63.34% of the variability in the dependent variable is explained by the independent variables in the study.

In addition, the results in Table 3 demonstrate that the model is statistically significant ($p < 0.01$), affirming the validity of the regression model used. This suggests that the variation in stock market performance, as measured by MPS, is effectively explained by the regression equation, validating the relationships among the variables under investigation.

The results, displayed in Table 3, indicated that four variables significantly influenced stock market performance: dividend per share (DPS), dividend payout ratio (DPO), retained earnings ratio (RER), and bank size (BS). Specifically, DPS had a positive and highly significant effect on MPS (β = 119.4232, p-value = 0.000), indicating that higher dividends per share are strongly associated with higher market prices. Conversely, DPO showed a negative and significant relationship with MPS (β = -34.68479, p-value = 0.026), suggesting that higher dividend payout ratios are associated with lower market prices. Similarly, RER had a negative and significant impact on MPS (β = -2.864767, p-value = 0.029), indicating that higher retention ratios are linked to lower market prices. Bank size (BS) also exhibited a positive and significant effect on MPS (β = 26.83039, p-value = 0.044), implying that larger banks tend to have higher market prices.

On the other hand, dividend yield (DY) did not make a significant contribution to predicting stock market performance (β = -1.324359, p-value = 0.254). The p-value for DY was higher than the threshold of 0.1, indicating that it is statistically insignificant in relation to the banks' stock market performance.

Discussion of Finding

According to Table 3, dividend per share (DPS) has a clear and significant positive effect on the market price of shares (MPS). This finding provides strong evidence against the first hypothesis, which posited that there is no relationship between DPS and the stock market performance of listed commercial banks in Nigeria. The significant positive coefficient indicates that as the DPS increases, the MPS also tends to increase, suggesting that investors respond favorably to higher dividend payouts. This relationship highlights the importance of dividend policies in influencing the stock market performance of commercial banks in Nigeria.

The results presented in Table 3 also demonstrate a significant impact of the dividend payout ratio (DPO) on the market price of shares (MPS). This finding leads to the rejection of the second hypothesis, which stated that there is no significant relationship between the dividend payout ratio and the stock market performance of listed commercial banks in Nigeria. The significant coefficient for DPO indicates that changes in the dividend payout ratio are meaningfully associated with changes in the MPS. This underscores the influence of dividend payout policies on investor perceptions and stock market valuations in the Nigerian banking sector, emphasizing that how much of earnings are paid out as dividends can significantly affect the market price of bank shares.

The retained earnings ratio (RER) also exerts a significant influence on the market price of shares (MPS) of listed commercial banks in Nigeria, as evidenced by the results in Table 3. Consequently, the third hypothesis, which proposed that there is no significant relationship between the retained earnings ratio and the stock market performance of these banks, is rejected. The significant impact of RER on MPS suggests that the proportion of earnings retained by the banks, rather than distributed as dividends, plays a crucial role in shaping investor expectations and stock valuations. This finding highlights the importance of retention strategies in determining the financial health and growth prospects perceived by investors in the Nigerian banking sector, and how these perceptions are reflected in the market prices of bank shares.

The analysis reveals that dividend yield (DY) does not have a significant impact on the market price of shares (MPS) of listed commercial banks in Nigeria, as indicated by the findings in Table 3. Thus, the fourth hypothesis, which posited that there is no significant relationship between DY and MPS, is accepted based on these results.

The non-significant coefficient for DY suggests that variations in dividend yield do not meaningfully affect the market prices of bank shares in the Nigerian context. Investors may not heavily consider dividend yield as a decisive factor when making investment decisions in the banking sector. This finding contrasts with the significant influences observed for dividend per share (DPS), dividend payout ratio (DPO), and retained earnings ratio (RER), highlighting that different dividend-related metrics can have varying impacts on investor perceptions and market valuations.

The analysis reveals that bank size (BS) exerts a significant impact on the market price of shares (MPS) of listed commercial banks in Nigeria, as indicated by the findings in Table 4.3. Therefore, the fifth hypothesis, which posited that there is no significant relationship between BS and MPS, is rejected based on these results.

The significant coefficient for BS suggests that larger banks tend to have higher market prices for their shares compared to smaller banks. This finding underscores the influence of bank size on investor perceptions and market valuations in the Nigerian banking sector. Larger banks may be perceived as more stable, with greater capacity to generate returns and withstand market fluctuations, thus commanding higher stock prices.

Conclusion

The results indicate that DPS is significantly associated with MPS, demonstrating a positive relationship. Similarly, DPO and RER were found to have significant positive effects on MPS, suggesting that higher dividend payouts and retained earnings ratios contribute to better stock market performance. Bank size (BS), used as a control variable, also showed a significantly positive effect on MPS, indicating that larger banks tend to perform better in the stock market.

However, the study found that dividend yield (DY) did not show any significant relationship with MPS. This suggests that while other dividend policy variables play a crucial role in influencing stock market performance, the dividend yield alone does not have a direct impact on the market price of shares for the listed commercial banks in Nigeria.

Recommendations

Based on the findings of the study, the following recommendations are made:

1. Deposit money banks should consider implementing a policy of regular dividend increases. This strategy can signal financial health and future growth prospects to the market. It can also attract a broader investor base, including those focused on income generation. By consistently increasing dividends, the company can enhance investor confidence and potentially boost stock prices.
2. Deposit money banks should focus on enhancing the company's profitability and operating cash flow. This can be achieved through strategic investments, cost optimization, and efficient operations. By improving these financial metrics, the company can afford to increase its dividend payout ratio.
3. Deposit money banks should carefully balance the allocation of profits between dividends and retained earnings. While distributing a portion of profits as dividends can attract income-seeking investors, retaining earnings to reinvest in the business can enhance the company’s long-term growth prospects and overall value. Effective use of retained earnings for strategic initiatives such as expansion, innovation, and debt reduction can increase the company’s assets and liquidation value. Clear communication about how retained earnings is being utilized to drive growth and

enhance shareholder value can help maintain investor confidence and support stock price appreciation

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