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Role of Dividend Policy in Determining the Market Value of Share Companies in Nigeria Stock Exchange

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Abstract: *This study examines the role of dividend policy in determining the market value of shares companies in Nigerian Stock Exchange. Dividend policy remains an important corporate financial decision because it determines the proportion of corporate earnings distributed to shareholders and the amount retained for future investment and business expansion. The study is anchored on Fundamentalist Theory, which emphasises the use of firms' financial and economic indicators, including earnings and dividend records, in assessing the intrinsic value and future performance of securities. The study adopts a qualitative research approach based on secondary data obtained from relevant published literature, including scholarly journal articles, books, corporate financial reports, and available records on dividend policy and share price performance. The secondary data were reviewed and thematically analysed to establish the relationship between dividend policy and the market value of shares. The review indicates that dividend per share, dividend yield and dividend payout ratio are important indicators associated with investors' perceptions and share price movements, although empirical findings remain mixed across firms and markets. The study further highlights the continuing debate between the dividend irrelevance perspective of Modigliani and Miller and the dividend relevance arguments advanced by scholars such as Gordon and Walter. It concludes that dividend policy remains a significant consideration in investors' assessment of listed companies and may influence the market value of shares, particularly in an imperfect capital market such as Nigeria.*

Keywords
Dividend policy; market value of shares; dividend payout ratio; dividend yield; dividend per share; Nigerian Stock Exchange.

I. Introduction

Dividend policy has been an issue of interest in financial literature since Joint Stock Companies came into existence. Dividend policy is a deliberate policy to maintain or increase dividend at a certain level with the ultimate aim of sustaining the price of the shares on the stock exchange. This is because capital markets are not perfect, and even though shareholders are indifferent between dividend and retained earnings due to market imperfections and uncertainty, they however, give a higher value to the current year dividend than the future dividend and capital gains (Simon et al., 2012). Dividend policy depends on investor's desire for capital gains as opposed to income, their willingness to forgo dividend now for future returns, and their perception of the risk associated with postponement of returns (Adefila, 2010). However, any normative approach to dividend policy intended to be operative under real world conditions should consider the firm's investment opportunities (Aondover, 2025).

Similarly, any preferences that investors have for dividends as opposed to capital gains and vice versa, and difference in "cost" between retained earnings and new equity issues should also be considered. Various firms adopt dividend policy depending on the company's articles of association, memorandum of association (in some situation) and the prevailing economic situation. Some make high pay out, while others make low pay out and yet others pay stock dividends (bonus issue) in lieu of or in addition to cash dividend while others pay

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cash only. All in a bid to maximize shareholders wealth which, in this case, is the market value of the firm's common stock (Adefila, 2010).

Dividends are commonly defined as the distribution of a share of profit among the shareholders of the firm in proportion to their ownership. Dividend policy can be defined as the payout policy, which managers use in deciding the size and pattern of cash distribution to shareholders over time (Sujata, 2009). Dividend is defined as that portion of the net earnings of the firm, which is distributed to the shareholders either in the form of cash or stock, as per its dividend policy. Dividend payment is usually part of the company's strategic policy to return a portion of its profits to its shareholders. The dividend ratio provides analytical information about the financial strength of the company or enterprises along with reflections about its investor's expectations. The dividend can be distributed either in cash or by capitalization of profit as bonus shares (Kehinde & Abiola, 2001).

Amarjit et al. (2013) defined dividend policy as payments made to stockholders from a firm's earnings, whether those earnings were generated in the current period or in the previous period provided declaration for the distribution of such profit has been made by the management. In simple statement, dividend could also be referred to as that part of the enterprise earning that is given to shareholders as return on their investment. A company pays dividend to reward existing shareholders and encourage others that are prospective shareholders to buy new issues of the common stock at high price. However, it is obvious that a firm would always want to give as much as possible to its shareholders by paying dividends. It might seem equally obvious that a firm can always invest the money for its shareholders instead of paying it out. According to Chinyere (2014), the question at the heart of dividend policy is should the firm payout money to its shareholders? Or should the firm take the money and invest it for shareholders to earn better return in the future?

Investors in underdeveloped countries like Nigeria mostly look at the profitability of the firm while purchasing equity shares from the secondary market. Since dividend paid to the shareholders is one of the best indicators of profitability it is generally believed that dividend plays a crucial role in determining market price of the corporate share (Okafor & Mgbame, 2011). The company generally pays stock dividend if it plans to increase the capital so as to expand the business. The primary objective of dividend policy should be to maximize the shareholders return so that the value of their investment is maximized. The firm issues equity shares to raise ownership capital and the investors buy them with the ultimate expectation to receive a share of profit as well as enjoy capital appreciation. The value of the firm is said to be high when the share price of the company's common stock is higher (Ashamu et al., 2012). Firms that perform better than others are expected to have higher share prices and can raise additional funds (both debt and equity) in more favourable contractual terms at the capital market than the others.

That is why Pandey (1999) firmly states that dividend policy is a decision by the financial manager whether the firm should distribute all profits or retain them or to distribute a portion and retain the balance. Therefore, the critical question in dividend policy is whether dividend has an influence on the market value of the firm, and a firm's investment decisions. Traditionally, managers pay attention to their choice of the dividend policy for the firm since they believe that dividend policy influence the value of their company and hence the wealth of their shareholders. Value is important for both companies listed on the stock exchange and those not listed (Gladys, 2007). Modigliani and Miller (1961) demonstrated the irrelevance of dividend policy under a set of assumption, that is, dividend policy has no effect on share prices. But when these assumptions are relaxed, the theory begins to disintegrate. Moreover, it has been discovered that the dividend policy of a firm always have short term or long term effect on the market price of its shares. Therefore, it is against this background that this study aimed at examining the role of dividend policy in determining the market value of share of listed companies in the Nigeria Stock Exchange.

1.1 Theoretical Context

The paper adopted Fundamentalist Theory. This is the statistical evaluation of stock prices using audit reports, profit and loss statements, balance sheets, dividend records, sales data etc to forecast future business conditions. Fundamental analysis involves an estimate of the intrinsic value of a security by evaluating the basic financial and economic facts about the company that issues the security. The intrinsic value is the present worth of the future dividends or earnings expected from the share. Once the intrinsic value is determined, it is then compared to the current market value. If the current market value is below the intrinsic value, a buy recommendation is issued as it is under-priced because the price of such share is expected to move up in future to match with the intrinsic value. In the other words, when the market price of a share is higher than the intrinsic value, the shares perceived to be overpriced and as such, the investor is advised to sell the shares. Okafor (1983) is of the view that fundamentalists use three basic performance indicators in predicting intrinsic values. These are the earnings record, index of risk and conversion rate for funds.

II. Research Methods

The study adopts a qualitative research approach based on secondary data obtained from relevant published literature, including scholarly journal articles, books, corporate financial reports, and available records on dividend policy and share price performance. The secondary data were reviewed and thematically analysed to establish the relationship between dividend policy and the market value of shares.

2.1 The Concept of Dividend

The concept of dividend has been defined by many authors and researchers. Bierman (2001) and Baker et al., (2002) have described it as an appropriation of profits to shareholders after deducting tax and fixed interest obligations on debt capital. Dividends are returns to shareholders from company earnings. A dividend is a cash payment from a company's earnings announced by a company's board of directors and distributed among stockholders. In other words, dividends are an investor's share of company profit, given to him or her as per owners of the company (Jones, 2005). Dividend payment could provide a signal to the investors that the company is complying with good corporate governance practices. Dividends are usually paid out of the current year's profit and sometimes out of general reserves. They are normally paid in cash, and this form of dividend payment is known as cash dividend (Aondover, 2025).

Dividend payment is a major component of stock return to shareholders (Zakaria et al., 2012). Dividend payout and dividend yield have been generally recognized as the proxies for dividend policy (Ramadan, 2013). Dividend payout (Ratio) is defined by Ramadan (2013) as the ratio of total cash dividend paid out to common stock holders to net income available for common stock holders. Dividend yield, on the other hand, is a profitability indicator expressed as a cash dividend per share for common stocks divided by the per share market value, i.e. dividend per share divided by the market value per share.

2.2 The Concept of Dividend Policy

Dividends can be paid in cash, products or as additional shares of stock. Stock dividends increase the number of shares outstanding and tend to generally reduce the price of each. Dividends can be announced at regular dividends to be paid at regular intervals or as a special dividend, paid only once. Liquidating dividends exceed earnings and might be paid to resolve part or the entire firm. Dividend policy, which involves itself in determining the amount to be paid to the shareholders and that to be retained in the company for future reinvestment in profitable projects or for other justifiable needs is one of the cardinal issues involved in financial management (Oyinlola & Ajeigbe, 2014).

The importance of dividend policy in the business world cannot be over-emphasized. A number of stakeholders, including investors, managers, lenders, financial consultants/analysts, etc. use it in making informed decisions. Considering the importance of dividend policy from the investors' point of view, dividend is not only a source of income but also a way to assess company from investment point of view. In other words, their main objective of investing in the stock market is to maximize the expected return at low level of risk, and this return may be in the form of dividends or capital gain. In effect, maximizing shareholders' wealth depends on the dividend policy of the company because of these shareholders would satisfy their purchasing and consumption patterns (Khan, 2012; (Aondover, 2025).

Dividend policy is a firm's policy with regards to paying out earnings as dividend versus retaining them for reinvestment in the firm. It is the division of profit between payments to shareholders and reinvestment in the firm. Dividend policy is thus an important part of the firm's long—run financing strategies. According to Nissim and Ziv (2001) define dividend policy as the regulations and guidelines that a company uses to decide to make dividend payments to shareholders. The dividend policy decisions of firms are the primary element of corporate finance policy. The major concern of the dividend policy is, of course, the trade-off between dividend payout and retained earnings. Dividend policy suggests a positive attitude for, it is a deliberate policy to maintain or increase dividend at a certain level with the ultimate aim of sustaining the price of the ordinary shares on the stock exchange.

According to Abdullah (2014), dividend policy is a major financing decision that involves payment to shareholders with respect to the return on their investments. Every firm operating in a given industry follows some sort of dividend payment pattern or dividend policy and obviously it is a financial indicator of the firm. Thus, demand of the firm's share should to some extent, be dependent on the firm's dividend policy. Dividend policy is an important aspect of corporate finance and dividends are major cash outlays for many corporations.

Dividends are usually paid out of the current year's profit and sometimes out of general reserves. They are normally paid in cash, and this form of dividend payment is known as cash dividend. Another option available to a company for the distribution of earnings is by stock dividend (bonus issue) which is supplementary to cash dividend. When cash dividend is paid to shareholders, it has an adverse effect on the liquidity position and the reserves of the firm as it tends to reduce both of them (cash and reserves). Unlike cash lend, stock dividend does not affect the total net work of the firm, as it is a capitalization of owners' equity portion.

Also, according to section 370 sub-section (1) of CAMA CAP C20LFN 2004, a company may in the annual general meeting, declare dividend only on the recommendation of the Directors. The Company may from time to time pay to the members such interim dividends as appear to the directors to be justified by the profits of the company. According to sub-section (3), the general meeting shall have power to decrease the amount of dividend recommended by the directors, but shall have no power to increase the amount recommended. While subsection (5) stated that, subject to the provisions of this Act, dividend shall be payable only out of the distributable profit of the company.

Furthermore, section 381 of CAMA states that a company shall not declare or pay dividends if there are reasonable grounds for believing the company is or would be unable to meet up with or pay its liabilities as they become due. Dividend policy suggests a positive attitude for, it is a deliberate policy to maintain or increase dividend at a certain level with the ultimate aim of sustaining the price of the ordinary shares on the stock exchange. This is because capital markets are not perfect, although shareholders are indifferent between dividend and retained earnings due to market imperfections and uncertainty, but they give a higher value to the current year dividend than the future dividend and capital gains.

Thus the payment of dividend has a strong influence on the market price of the shares. Management might maintain a dividend level even at the expense of liquidity or forced into borrowing to do so. With this approach it holds that dividends, on the other hand, are desirable from the shareholders point of view, as increasing their current wealth and consequently dividend level determines share price as well as indicates the prospect of profitability of the firm.

On the other hand, profit retention policy tends to suggest a more passive residual attitude towards dividend, that is, a passive attitude towards retention. Dividend payout reduces the amount of earnings to be retained in the firm and affect the total amount of internal finance. When dividends are treated as a financing decision, the net earnings of the firm may be viewed as a significant source of financing the growth of the firm.

Dividends paid to shareholders represent a distribution of earnings that cannot be profitably reinvested by the firm. The approach to dividend is viewed merely as a residual decision. This theory is known as the residual theory of dividend and was first proposed by Miller and Modigliani in (1961). Investor prefer to have the firm retain and reinvest earnings rather than pay them out in dividend if the return on the investment earnings exceeds the rate of return the investors could themselves obtain on other comparative investment. Otherwise, the investors prefer dividend.

In the absence of taxes, transactions costs and other capital market imperfections, Miller and Modigliani (1961) show that dividend policy should not affect shareholder wealth. A N5 dividend payment made by the firm reduces assets by N5, reducing equity by N5. Since shareholders received the dividend, this payment exactly offsets the decline in equity value. On the other hand, corporate shareholders receive an 80% deduction for the dividends that they receive from other corporations and many non-profit institutions are tax exempt. These organizations often prefer holding shares in high payout corporations. Thus, the value of a company's stock may be some function of a clientele effect (Teall, 2014).

Brav et al. (2005) surveyed 384 CFOs to evaluate how they determine dividend and share repurchase policy. Their results indicate that historical dividend levels are most important in setting dividend policy (along with a desire not to cut dividends) and that dividends do convey information. Dividends were smoothed relative to EPS and were related to long-term changes in profits. In fact, they found that managers tended to focus more on the effects associated with changes in dividend levels than on the dividend levels themselves. Dividend tax rates relative to those of capital gains were less important, and the current stock price and EPS levels were unimportant. In many respects, corporate share repurchases are similar to corporate dividends.

III. Result and Discussion

3.1 Relevance of Dividend

Modigliani and Miller's school of thought holds restrictive assumptions on their argument regarding the relevance of dividend theory. They asserted that since; in reality investor operate in a world of brokerage fees, taxes, and uncertainty, it is better to view the firm in the light of these factors. The leading proponent of the relevance of dividend theory, Gordon (1962) suggests that shareholders do have a preference for current dividends, that, in fact there is direct relationship between the dividend policy of a firm and its market value. Gordon argues that investors are generally risk-averters and attach less risk to current as opposed to future dividends or capital gains. This "birds in hand" argument suggest that a firm' dividend policy is relevant since investors prefer some dividend now in order to reduce their uncertainty (Aondover, 2025).

When investors are uncertain about their returns they discount the firm's future earnings at a low rate therefore placing a higher value on the firm. On the other hand, Walter

(1963) is of the opinion that dividend policies in most cases do affect the value of the firm. The effect of the optimum dividend policy on the relationship between the firm's internal rate of return (r) and its cost of capital (k) according to him, is a growth function of the firm where 'r' is greater than 'k' (r>k), all earnings can be reinvested, hence, the firm is assumed to have sample profitable opportunities so as to maximize the value per share over and above the rate expected by shareholders. In a normal firm where r=k, dividend policy has no effect on the market value per share since the rate of return is equal to the cost of capital (Harry & Steven. 1994). In a declining firm where the optimum payout ratio should be 100% to enable increase in the market value per share, Walter expressed this as thus:

$$P = D/K + r(E - d)/K/K$$

Where

P = Market value of the share

E = Earnings per share

K = Cost of capital

r = internal rate of return

d = Current dividend

This Walter theory has been criticized because r and k are not constant in real life situation. Moreover, the non-existence of external financing makes it weak. The firm's r decreases as more investment occurs and k changes directly with the firm's risk. It should be understood here that

Walter's model though weak, recognizes the fact that dividend policy is relevant (Samuels & Wilkes, 1975). The owners of a company share are entitled to a revenue stream of dividends. The value of the share corresponds to the present value of this steam of dividends payments. Obviously, there is considerable uncertainty surrounding the size of the future dividends, indeed it is as a result of change expectations about future dividends that share prices fluctuate.

The owner considers his returns as accruing not just from dividend payments but from the additional gains resulting from any capital appreciation on the share. Normally he does not intend to hold the share in perpetuity, he wishes to sell the share and obtain capital gains, but when he sells the share, the buyer is also simply purchasing a stream of future dividend expectations. The reason the capital gain expectation arises is because of expectation about future dividend stream rise between the time when the investor purchases the shares and when he sells them.

Empirical Studies on Dividend Policy and Market Value of Shares

In previous studies, although there are variations in the findings on the relationships between dividend policy and share price, unlike these previous works; the scope of this research encompasses the influence of share price on dividend payout ratio, dividend yield and dividend per share. The findings on the relationships between dividend policies on share price are inconclusive. Furthermore, there are mixed findings on the relationship between dividend policies on share price.

Nigerian Studies

The issue of dividend policy did not receive any serious attention among academic scholars in Nigeria until 1974. Oluntoyin and Obadebo (2009) study the impact of companies' shares on their performance, using one of the largest confectionary companies in Nigeria as a case study and recommends that the confectionary company should implement policies that will encourage increase in their profit after tax, dividends and turnover as these variables have positive and statistically strong significance on the changes in the company's performance and the value of its market capitalization (Aondover, 2025).

Okafor and Mgbame (2011) conducted a study to analyses dividend policy and share price volatility in Nigeria by taking sample of 4 banks and 2 firms each firm food and beverage; Petroleum and brewing sectors. Stock &financial related data of these firms are collected over 8 year period from1998-2005. Major sources of data collection annual fact hook of Nigerian stock exchange. Dependent variable price volatility and independent variable dividend yield, payout ratio, assets growth and earnings volatility. The relationship between ordinary stock price volatility and dividend policy has been analyzed utilizing multivariate least square regression. The result of their study show that general effect of dividend yield on price volatility observed at higher significant levels.

Ashamu et al. (2012) study investigated the effect of dividend policy on the value of the firm. It examined relationship between dividend payment and payout ratio and found out the percentage of earnings to be retained or ploughed back into the company and identified the various factors that determine the pricing of shares. Osamwonyi and Evbayiro-Osagie (2012) study the relationship between macroeconomic variables and the Nigerian capital market index and found that macroeconomic variables influence stock market index in Nigeria. It is recommended that the adoption of appropriate economic policies will be beneficial to the stock market index [a proxy for stock prices] and this in turn will result in needed growth in the capital market. It has been observed that pricing of securities in the capital market is a mixture of qualitative analysis and forces of demand and supply. Price movements in the Secondary market are determined in the main by the forces of demand and supply.

Ordu et al. (2014) examined on the effect of dividend payment on the market prices of shares in Nigeria: A study of 17 quoted firms using time series on dividend per share, dividend yield and dividend payout ratio that ranges between 2000 and 2011. The model specification for the analysis of data is ordinary least squares techniques applied as panel estimation. The researchers empirical results arising from the panel least squares suggests a positive effect between market price per share and dividend per share confirming that a rise in dividend per share brings about an increase in the market price per share of quoted firms; that dividend yield does not have a significant positive effect on the market prices of shares of quoted firms in Nigeria; that there exists a direct relationship between market prices per share and dividend payout ratio of selected firms on the NSE. Further, the study revealed that significant variations exist in the movement of the share prices of the selected firms which in theory could be attributed to the forces of demand and supply while in practice could be attributed to some other exogenous and endogenous variables such as economic policies, corporate managerial decisions, psycho-social variables, political situations and institutional parameters.

3.2 Studies from other Jurisdictions

There are many number of studies conducted worldwide with respect to dividend policy and share price fluctuation. The earliest major attempt to explain the dividend behaviour of companies has been credited to Lintner (1956) who conducted this study on American companies in the I950s. Since then there has been an ongoing debate on dividend policy in the developed markets resulting in mixed, controversial and inconclusive results.

Rashid and Rahman (2006) introduced the dividend policy and stock price volatility in the context of Bangladesh. The aim of the study is to investigate the relationship between dividend policy and share price olati1ity. For this purpose they consider the data for the period of 1999-2006. The selected the sample of 104 non-financial firms of different sectors listed in Dhaka stock exchange. The authors used descriptive statistics and cross sectional regression analysis to conclude the results. The Pearson's correlation showed that there is negative significance correlation between payout and price volatility.

Asghar (2011) conducted research on effect of dividend policy on stock price risk in Pakistan. The study checks the relationship between dividend policy and stock prices. Using five important sectors i.e., chemical, cement, Sugar, engineering, synthetic & fiber for the period 2005-2009 from the published resources of state bank of Pakistan and Karachi stock exchange. Price volatility is taken as dependent variable while dividend yield, dividend payout price ratio, earning volatility and growth in assets are taken as independent variables.

Regression model based on Baskin (1989) documentation was used to conclude the results. The results of this study prescribe that Price volatility has strong positive correlation with dividend yield but PV is highly negatively correlated with growth in assets.

Habib (2012) conducted a study on dividend policy & share price volatility evidence from Pakistan. To draw and establish the relationship between dividend policy and shareholder volatility with focused on Pakistani stock exchange. Dividend yield, payout ratio, size, debt, earning & growth independent variable & share price volatility dependent variable. Cross sectional regression use to analyze relationship of share price with dividend yield & payout ratio. The result of this study show that dividend yield & share price positive relate but payout ratio is negative related.

Hashemijoo (2012) conducted the study of dividend policy on share price volatility in stock market of Malaysia. The aim of this study was found that the relationship between dividend policy and share price volatility on consumer product company in Malaysian stock market. They have taken a sample of 84 listed companies from the period of six years in 2005 to 2010. The results of this study show that the dividend yield or dividend payout has negative effect in share price volatility.

Profilet and Bacon (2013) conducted the research on dividend policy and Stock price instability in the U.S equity capital market. The purpose of the study is to identify the impact of certain financial variables on the stock price instability. It was found out that leverage and growth both have negative relationship with stock price instability and there is positive relationship observed between the payout ratio and the stock price instability. Almumani (2014) examined the quantitative factors that influence share prices for the listed banks in Amman Stock Exchange over the period 2005-2011 using empirical analysis of a set of independent and dependent variables and found that there is a significant positive relationship between EPS and the MP of the listed banks in Jordan.

IV. Conclusion

The paper concludes that dividend policy plays an important role in determining the market value of shares of companies listed on the Nigerian Stock Exchange. The review of secondary data and existing literature indicates that dividend per share, dividend yield and dividend payout ratio can influence investors' perceptions, investment decisions and movements in share prices. Although the findings of previous studies remain mixed and the debate between dividend relevance and dividend irrelevance persists, the evidence suggests that investors in the Nigerian capital market often attach considerable importance to current dividend returns as an indicator of corporate performance, profitability and financial stability. Consequently, companies need to formulate dividend policies that appropriately balance the interests of shareholders with the need to retain earnings for profitable investment and sustainable growth. A well-designed dividend policy can strengthen investor confidence, enhance the attractiveness of a firm's shares and potentially contribute to the improvement of its market value. The study therefore concludes that dividend policy should be treated as a strategic corporate financial decision rather than merely a mechanism for distributing profits, particularly within the imperfect and developing capital market environment of Nigeria.

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