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Legal Impact of Distribution of Dividend Policy on Share Price in Pakistan

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Abstract: *This empirical study examines the controversial relationship between dividend policy and stock prices on the Pakistan Stock Exchange while considering legal implications. Sample data for 18 listed commercial banks (2012-2019) were collected from financial sources. Panel data analysis and several regression models (random effects, fixed effects, and Hausman test) were used. The study shows that cash dividends and dividend yields have a large impact on stock prices, while variables such as earnings per share, retention rates, and after-tax earnings do not. This result contributes to our understanding of the Pakistan stock market and is relevant to emerging and developing markets. However, there are limitations such as high market prices, dividend volatility, and occasional non-payments leading to the issuance of bonus shares by commercial banks.*

Key Words: Share Price Volatility, Corporate Dividend, Dividend Yield, Hausman Test and Legal Impacts

Introduction

Corporate finance has many fundamental roles in a capitalist economy and it represents the overall growth of the system. Financial markets are divided into two segments ie Money Market (short-term) & Equity Market (long-term). Stock Exchange is the financial market in which investors buy shares against the dividend or capital gain to maximize their profit legally governed under SECP Rules. The share price is the reflection of the investors and it varies year by year and operation by operation. The return which is given to shareholders or preferred stockholders is known as a "Dividend" in finance.

In a high-earning period share price is increased and its sales are stable, also maintaining benevolence in the eyes of investors and vice versa. Successful companies carn high income and it depends on their policies to pay dividend or retain it for future projects. Dividend payout, earning per share, net on investment share price fluctuation and so on all these variables have a great impact on share price volatility and dividend payout. Many studies have been conducted to find which variable has a strong effect on the inconsistency in the share price. Some schools of thought believed that has no impact on share price volatility or the value of the firm while others have different views regarding the same measures.

The objectives are achieved by improving the firm as well as formulating smart strategies. Efficiency makes the benevolence of the firm and informed the shareholders about the value of the firm. Investors have gained confidence in the company when they communicate the right information to them and allow them to analyze the current earning of the firm. Shareholders want to maximize their wealth and make their firm earn high and stable ales with growth. The firm has to develop policies on whether all the net income should retain or payout to their investors or make some percentage between both finances.

Legal Dividend Policy has the most essential role; it has great significance in the field of finance. Investors prefer Dividends more than capital gain as their stability is prudent. To maintain stability firms usually increase the Dividend payout, its share price increases

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as well and the cost of equity decreases. Dividend Policies are not set in stone, they may be changed according to conditions and after seeking out the macro environment risks. Investors' behaviour is also changed regarding the policies. A dividend Policy is all about the management decision which is taken by the finance manager for the development of the company and also the value of the firm. Relax, Aggressive or Conservative decision-making policy is taken by the firm after the analyses of the situation.

Inaccurate decision makes the company unbalanced and they have to face a loss. Dividend policy is the most single area for the management to attract investors more to obtain funds and stick them with enterprise

Investors' preferences play a great role when the decision is taken by finance managers. Because some investors want high dividends and increased share price while others talk about the growth of the firm. Capital structure, coming rate, stability, goodwill. Credit standing, share price and other policies are interlinked with each other and the most prominent is the Dividend Policy which makes the investors take for holding the shares or sell it out to take capital gain. Most investors want high dividends as well as increased share price rather than capital gain. The firm's main objective is to maximize shareholder wealth and it is only possible when the firm takes the balanced and smart decision making to satisfy them in order to give them consistent dividend payout and also make work to increase the growth and improve the performance of the firm.

The dependent variable is found to be Share price, whereas Independent Variable is found as Payout Ratio, Dividend Yield, and Earnings per share, Profit after tax

Significance & Objectives of the Study

The article aims to find the relationship between the share prices and the dividend policy of the firm in the Pakistan Stock Exchange... Its impact on the share market price and value of the firm. In finance share price and dividends are the most controversial topics, many academic institutions have debated on it but no final conclusion arises still. Two different opinions make it more mysterious which is why this topic has great importance.

The dividend is one of the most important measures at the time of investment. It gives a signal to investors about the performance and health of the firm. The share price is volatile in a variety of ways e.g. market sentiments, macro environment, and internal and external formulation of strategies and financial behaviour of the market. Shareholders are concerned about the return on their investments and bear risk. Earning of the firm is diluted at the time of dividend payment, those firms that have a high payout ratio tend to have less growth orientation rather those who have a high retention rate which is opposite to the payout ratio. Investors attract to invest in those companies that have high and stable rates of return, also risk is minimised

A consistent approach in dividend policy is sustainable not only for companies but also for investors. This approach brings an increment in the share price and attracts investors with a stick. At the time of the declaration of the dividend, the firm gives a signal to investors and also encourages them to buy more stocks with a premium. It tends to increase the share price and enhance the value of the firm. Many variables greatly impact the share price, most importantly profitability ratios e.g. cash dividend. A stock dividend, dividend yield, and earning per share. Price to comings ratio, return on equity. Debt ratio, profit after tax and so on. The investors are paid cash as a return while in stock dividends they are paid stocks as a return. Earnings per share are also a good measure to know how much the company cares about each share. Retention rime is used for growth and diversification. RR is opposite from payout because as the payout increases then RR decreases.

Firms make strategies according to the financial behaviour of investors. Profit after tax is variant in each financial year which is highly influential for dividend and share price because the dividend is paid or retained in net income, and the formulation of policy hits share market price.

Scope and Limitations of the Study

- Capital investment, business advancement and allocation of resources in the financial markets
- Borrowers and lenders are facilitated by the offered services and policies
- Financial markets have a consistent approach and symmetric reflection to boost economies.
- Diversification and expansion of businesses attract investors with increased spending pattern
- Capital structure is maintained according to the macroeconomic condition
- Cash flows should have consistent streams to achieve the benchmarks.
- Sustain corporate dividend policy brings stability to the financial market as well as to the economy

- Patterns are consistent in approaching the behaviour and investors' perception
- Transparency is the first priority at the time of declaration of the dividend and financial policies.
- Liquidity is included which helps the investors to make capital appreciation in the secondary markets.

Delimitation of the Study

- Tax structure and audit financial systems are vast and have the red flag.
- A high level of risk is involved to invest
- Instability is sought in the Pakistan Stock Exchange Markets which brought risk-avoiding patterns
- Government interference is there to report the operational available business activities.
- The momentum about investment is clearly maintained in the premises of fundamental analysis.
- Payment of dividends should be correctly declared at the time of investment for holding.
- The presence of inconsistency in PSX makes it more volatile for investment and growth.

Literature Review

Theoretical Framework

Dividend policy is one of the most contentious, observed and conceptual topics in the field of finance. Stock markets are considered as the barometer of the capitalist economy. In corporate finance Share prices are the reflection of any firm and investor behavior is rational at the time of investment in a particular company. Free enterprises float their shares in the stock market and give returns to stockholders as "Dividend'. The net income of an Enterprise is divided into two parts Dividends and Retained Earning'. When Firms distribute 100% Dividend (payout) to shareholders from net income. It means cash outflow increases, and with that chances of the share price are also increased but growth or development is decreased. In contrast, if Firms retain (100% retention rate) all the net income, and cash outflow decrease, changes in share price decrease but growth or development is increased. These two different extremes make the stock price and dividend policy controversial Optimum policy where maximum profit is provided makes the Dividend stabilize and grow the share price as well as the value of the firm.

This topic is determined to investigate and remain in discussion. Many studies have been conducted to find the reasons for fluctuations between both but the results are different. In an efficient market, an investor makes the difference between the actual dividend increase and the artificial dividend increase.

Dividend and Stock Price fluctuations are generated by the different capital structures because the dividend is linked with stock price and its impact is pronounced. It should be consistent and stable. People avoid risk and if they take risk then they consider it should be less. The stock price is the gauge to determine risk whenever making an investment. Many circumstances are involved in the volatility

Like political inconsistency, economic issues, and social problems cite. That makes a direct or sudden change in the policies and that is also a reason not to find the actual measures behind the inconsistency. Pakistan Stock Exchange is a herd effect market and it has been observed that there is a huge gap in stock and dividend because of asymmetric information. Pakistan Stock Exchange is a weak form of an inefficient market. The performance and value of the firm depend upon efficiency in Stock Price and also Dividend

In Corporate Finance Shareholders want to maximize their wealth and it is only possible when the firm maintains its stability and nourishes consistent profitability by giving its investors an efficient platform. To attain this there is a conflict between increased share price and growth at the same time. And this makes it controversial and creates issues that bow to getting both extremes in the same manner. There is a positive relationship between the payout ratio and increased share price or a negative relationship between retention rate and stock price. Many theories postulate and studies have made to main both no exact finding, score for many years. Dividends are given to stockholders. And it is dependent on capital structure, capital budgeting, strategies, macro environment condition and so on. Dividend policy and stock price decisions are taken on informed judgment after seeking out all the above circumstances not by applying statistical or logical equations. Both have great importance in the field of corporate finance and also in the lassie faire economy. It is also observed that at the time of dividend announcement, the share price change in the very next second and that change may be increased or decreased and the price is brought inconsistency in Pakistan Stock Exchange because that change is swift. This is also a reason makes the PSX inefficient because of asymmetric information

Basically, inconsistency comes from an inexact decision. The questions that may occur problems are how much dividend payout to stockholders, firm also faces problems in regard to following the steady growth or should increase their share price, or maybe the growth (expand) business by retention. Dividend and Stock price fluctuations have been empirically tested by many researchers in Relevance or Irrelevance theories.

Legal Impact of Dividend Policy on Share Price

Many studies are conducted on volatility. Researchers have made many contributions to the most contentious issue in the field of finance. Dividend and Stock price fluctuation are held a healthy debate in most academic circles. Its effect, some. Strategic matters a lot in the growth of a capitalist economy and value...

The first school of thought who presented the Irrelevance Dividend Theory was Merton Miller and Franco Modigiami (MMP in 1960. They argued that Dividend Policy is irrelevant. A company's value is only dependent on its earning and the way they distribute it among shareholders. If brokerage fee and tax is eliminated then Dividend Theory becomes irrelevant. Many assumptions and properties were presented to make validity that it is irrelevant

Another school of thought were Myron Gordon and John Lintner (1963) who disagreed with the Inelegance Theory of (MM), according to them The Dividend Theory is Relevant because investors want to secure their income and minimize their risk so as to attain the firm increase dividend payout ratio to attract more investors and obtain funds. Investors are much concerned about the value of the firm and income because they want to maximize their wealth It means that the Dividend Policy affect the stock price and value of the firm. Fama (1991) and French 1992) centre of attention was dividend, stock price and other variables that affect and make reason of volatility, they also explain stock returns.

In 1996 Allen and Rachin conducted a study of the riskiness of stock price and dividend payout and found negative relation. They also found that the capital structure and magnitude of the firms inspect stock prices as well. Many researchers give a favour that stock price is not affected by dividend policy. Myers & Frank (2004) made research on it and appeared that stock price and dividends have positive relationships. Baker, Mukherice, & Paskelian (2006) described that there is an assorted judgment after the findings. Amidu and Abor (2006) used panel data of 20 companies which wits listed on the Ghana Stock Exchange and found that there is a negative relation between payout and set escorted. Rashid and Rebman (2008) performed a study to find the link between dividend and stock price volatility in Bangladesh and appeared that there is a positive relation between both in Dhaka Stock Exchange. In 2001 Nishat and Itfan conducted a study on Pakistan Stock Exchange and found the effect of dividends on the stock price. In 2001 another study was appeared by Nazir et al on the non-profit organizations listed on Pakistan's Stock Exchange

Panel data was applied and found a negative relationship between both estimation of dividend and stock price fluctuation. Khan et al (2011) also conducted the impact of volatility of both and try to find whether they are relevant or irrelevant to cash other, to obtain this collected 55 nonprofit organizations listed in Pakistan Stock Exchange used panel data on their study and found the correlation of negative relation with retention rate and share price Vespasian. Massy studies are conducted to find the fluctuations but there is a contradiction among the results, and the question remains that Dividend payout and Stock price are relevant or irrelevant.

Corporate law authorizes the board to decide company matters since the responsibility is upon the directors to protect the company properties and the rights of stockholders, staff and creditors, but a large no of participants questioned the unchecked authority of the board. The directors give the reason for retaining cash to expand plants or to invest in new ventures; it can be a valid reason. As investors are likely to exit the market if they do not get reasonable profit from their investments. As of now, almost 50% of the listed firms are not paying dividends to their stockholders. A recent report released by a research house, Optimums Capital Management.

However, the number of companies that distributed dividends to shareholders has considerably reduced from 256 in 2018-19 to 217 in 2019-20 and 180 in 2020-21. The total amount paid to investors n dividends amounted to Rs. 357 Bn, Rs. 308 Bn and Rs. 381 Bn respectively for the above three years.

Commercial banks are the highest dividend payers amongst all the listed sectors. However, the banks' payout had considerably dropped to Rs. 88 Bn for the year 2019-20. During the pandemic, the State Bank of Pakistan directed all banking companies to suspend the distribution of profits by way of oil dividends for the quarters ending June 30, 2020, and Sept 30, 2020. This act was the major reason for dropped bank payouts. State Bank of Pakistan explained this act "to conserve capital and further enhance the lending and loss absorption capacity of banks." As the pandemic situation improved state Bank of Pakistan lifted the ban on the suspension of Dividends and as a result, banks distributed healthy dividends of Rs.104 Bn for the year 2020-21

Data Collection and Methodology

The quantitative research method is used in this study. The banking sector of Pakistan is the population of this study. 18 listed bank of the stock exchange is used as sample Convenience sampling technique is used. Data is collected from the Pakistan stock exchange. State Bank of Pakistan websites, Business recorders and websites of sample banks and has reliability. Quantitative data is collected to see the relationship between share prices with other variables.

Econometric Model

This article crude the relationship between share price and cash dividend, dividend yield, retention ratio, earning per share and profit after tax to measure these regression models used.

Panel data is used to measure the impact of corporate dividend policy on share price volatility. Fixed effect model and random effect model are taken. Both models have their own properties. The fixed effect model is used to see the effect of dividends on share market price after controlling the influential variables. In the fixed effect model, it is assumed that all banks have the same patterns but investors have different perceptions to take the risk. For this consideration, the Random effect model was also applied to the study because all the companies have different sizes, capital structures, growth policies, and investors Results are taken on the basis of statistical instruments and those are coefficients, t-statistics, p-statistics, F-statistics, R^2 and Adjusted R^2 also Durbin Watson Test is applied. To see the impact among variables. The Housman test is applied to the data whether the fixed effect model is appropriate or the random effect model. The significance and Insignificance of p-values show the appropriation of the results. Penal data collected from 2012 to 2019 is valid for the study.

Result and Discussion

Table 1

Descriptive Statistics

	SP	DIV XI	BET X2	D.Y X#	PAT X5	EPS X4	DIV XI
Mean	52.87910	3.323958	-4.216051	0.048373	8060157	6.067639	3.323958
Median	22.21000	1.875000	0.601487	0.51273	5287335	6.620000	1.875000
Maximum	285.3500	17.00000	1.00000	0.182648	35470458	23.93000	17.00000
Minimum	0.790000	0.00000	-699	0.00000	-5377240	-4.27	0.000000
Std.Dev	66.76005	4.5113%	58.30447	0.45463	8676432	6.823559	4.511396
Skewness	1.683800	1.550242	-11.87406	0.438914	0.999679	1.186038	1.550242
Kurtosis	4.874357	4.354144	141.9980	2.310757	3.177107	3.387680	4.354144
Jerque-Bera	89.12370	68.68028	119306.5	7.473822	24.17278	34.66225	68.68028
Probability	0.000000	0.000000	0.000000	0.023828	0.000006	0.00000	0.00000
Sum	7614.590	478.6500	-607.1113	6.965722	1.16E+09	873.7400	478.6500
Sum Sq.Dev	637337.3	2910.435	486115.9	0.295561	1.08E+16	6658.217	2910.435
Observation	144	144	144	144	144	144	144

Table 2

Unit root test

	LLC	IPS	ADF	PP	Inference
SMP	0.00	0.00	0.00	0.00	Stationary
DIV	0.00	0.00	0.00	0.00	Stationary
Div. Yield	0.00	0.00	0.00	0.00	Stationary
EPS	0.00	0.00	0.00	0.00	Stationary
RR	0.00	0.00	0.00	0.00	Stationary
PAT	0.00	0.00	0.00	0.00	Stationary

Table 2 described that the Unit root test is applied to check the stationary among variables. Share market price,cash dividend, Dividend Yield, Earning per share, Retention Rate and Profit after tax are taken to find the impact. For test Levin, Lin & Chu t' test (LLC), Im. Pesaran & W-stat (IPS), Augmented Dicke y Fuller

(ADF) and Fisher Chi-Square (PP) test are applied. At a 5°/c level of significance, the null hypothesis at level is rejected due to non-stationary y between two explanatory variables (EPS and PAT). The result was mixed. Focus on the same high results and applied them. At the first level, the result is the same. At the second level difference, all the variables are stationary and there is no unit root exists.

Table 3

Correlation Matrix

	Sh. Price Y	Div X1	D.Y X2	EPS X3	Ret X4	PAT_X5
Sh. Price Y	1					
Div X1	0.927689	1				
D.Y X2	0.254157	0.453324	1			
EPS X3	0.908312	0.907872	0.354532	1		
Ret X4	0.005252	-0.071957	-0.194829	0.071695	1	
PAT_X5	0.844548	0.858928	0.447717	0.937923	-0.076615	1

- Table 3 describes that there is a positive correlation between share market price and dividend which is statistically insignificant to 5°/o level of significance. As companies offered high dividend rates to investors their share market price increases with the value of the firm and at the time of low dividend rate is offered to investors it will obtain a decrease in share market price in the listed stock exchange. Share market price and dividend yield have a weak correlation that is (0.254) which is in line with Allen & Rachim's (1996) study in the Australian market found a positive correlation but contrast to Baskin's (1989) US stock market found a negative correlation and Hussaine y et al in UK stock market also found negative results between share market price and dividend yield. As the share market price increases, dividend yield does not follow the same pattern with SMP which is why they have a low correlation in emerging stock markets. SMP and EPS have a strong positive correlation (0.908) which means that as the share price increases, firms' earnings in regard to the price also increase.
- The result supports the literature which is mentioned in the article. RR is the opposite of PY.In the result SMP and RR has the least correlation (0.005) which means that asthefirm has a high retention strategy, itsshare market pricedecreasesand does not havedirect flow in the listed stock exchange market. The last variable implies that SPV and PAT have a positive correlation (0.84) which means as the net income increases thecompany is able to pay high dividends to its investors and as a result its share market price increases.

Table 4

Fixed Effect

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	44.32198	4.0947	10.82423	0
DIV_X1	8.413115	1.109227	7.584665	0
D_YIELD_X3	-390.2335	62.22874	-6.270954	0
EPS_X4	-1.129086	1.753605	-0.643865	0.5209
RETENTION_X2	0.013873	0.030306	0.457766	0.6479
PAT_X5	7.91E-07	1.25E-06	0.635191	0.5265

- Table 4 describes that fixed effect model dividend and dividend yield have a significant impact on the share price. Positive relations were found among dependent and explanatory variables which are similar to Nazir, Nawaz, Anwar & Ahmed (2010) but not similar to Baskin (1989). The retention ratio is insignificant to share price which is also similar to them but not with Pani's (2008) results. Negative relation shows that in Pakistan investors want a high payout ratio rather than growth of the firm also as the share price increases retention ratio moves in a negative direction which means does not impact the share price. Earnings per share and profit after tax are insignificant to the share market price which is not consistent with the Adesola & Okwong (2009) results. Negative results show that profit does not impact share market price. Shareholders are only concerned with the return as a dividend whether it is paid from current net income or previous one.

Table 5

Random Effect Model

Variable	Coefficient	Std. Error	t- Statistic	Prob.
C	16.89009	2.897314	5.829567	0.000
DIV_X1	10.86247	0.840572	12.92271	0.000
D_YIELD_X3	-336.4535	42.75319	-7.86967	0.000
EPS_X4	2.206623	0.993469	2.221128	0.028
RETENTION_X2	-0.001638	0.026489	-0.061852	0.9508
PAT_X5	3.43E-07	6.53E-07	0.524546	0.6007
R-squared	0.840210	Mean dependent var	34.44249	
Adjusted R-squared	0.834421	S.D dependent var	45.58662	
S.E of regression	18.54985	Sum squared resid	47485.39	
F-statistic	145.1269	Durbin-Watson stat	1.188859	
Prob(F-statistic)	0.000000			

- Table 5 is showing that the random effect model dividend and dividend yield have a significant impact on the share price. Positive relations were found among dependent and explanatory variables which are similar to Nazir, Nawaz, Anwar & Ahmed (2010) but not similar to Baskin (1989). The retention ratio is insignificant to share price which is also similar to them but not to Pani's (2008) results. Negative relation shows that in Pakistan investors want a high payout ratio rather than growth of the firm. Earnings per share are significant to share market price which is consistent with the Adesola & Okwong (2009) results. Profit after tax is insignificant to share market price which shows that profit does not impact on share market price. Shareholders are only concerned with the return as a dividend whether it is paid from current net income or previous one.

Table 6

Correlated Random Effects- Hausman Test

Test summary	Chi-square statistic	Chi-sq d.f	Prob
Cross section random	77.385	5	0

Table 6 is showing that the Hausman test shows a significant result for the random effect model and insignificant for the fixed effect model which means that the fixed effect model is appropriate regarding the data. The goodness of fit is 0.94. Focused the fixed model effect on the basis of the Hausman Test Model. Results do not confirm the dividend irrelevance theory (MM)[2] (1961) but support Gordon and Lintner (1959), Dong, Robinson Thaler (1997), Veld (2005) and Brav et al (2005), DeAngelo & DeAngelo (2007), Rashid & Rahman (2009), who suggest the positive relationship between share market price and corporate dividend policy of the firm. In Pakistan or other emerging markets find the dividend in their investments whether it is in the form of stock or cash. Many factors bring change in company policies and strategies which directly or indirectly affect the share prices and other measures of the firm. Investors in the Bank of Pakistan shows a preference for dividend which makes it relevant for the share market price despite capital gain. Results show that stockholders' attitude towards dividends is positive with share market price in emerging or Pakistan Stock Exchange Market. Dividend policy plays an important role in explaining the dividend policies in light of investors' preferences and also their perceptionsor behaviour.

Conclusion

In this article, it is aimed to find the relationship between the stock price and corporate dividend policy governed under Legal Framework defined by SECP, in emerging markets and for this quantitative data is used and collected for the period of 2012 to 2019 of listed commercial banks in the Pakistan Stock Exchange. The convenience sampling technique is used and the sample size is 18 the data is collected from the State Bank of Pakistan, the Pakistan Stock Exchange and the Annual Financial Report of Banks to find the Legal Impact of "Corporate Dividend Policy" on the share market price of the firm. Explanatory variables are cash dividend and dividend yield while controlling variables (Earning per share, profit after tax, retention rate) are taken to see the impact. Panel data is used in which fixed and random effect is applied. Both approaches showed the positive results of cash dividend and dividend yield on the share market price of the firm. In the fixed effect model earning per share, profit, after tax and retention rate are negatively impacted on share market price and in the Random effect model earning per share, is positively impacted while retention rate and profit after tax are negatively impacted on share market price. Hausman test is applied for the selection. This test suggested the fixed effect model appropriation. This article and its results are valid for emerging countries like Pakistan, but not for developing countries. It is concluded that cash dividend and dividend yield have a significant impact on share market price while EPS, PAT and RR have insignificant impact and these variables are changed with the market changes.

Recommendations

- Corporate managers minimize the volatility of share price by controlling the cash dividend's payout or retention ratios.
- By reducing the share market price firms increase the dividend and obtain more funds.
- Investors have their own preferences regarding tax, return and investments they get benefits from this study and construct portfolios.
- A consistent approach should be adopted in the dividend to stick investors with thefirm.
- A stable share price enhances the confidence of investors and reduces the volatility of the firm.
- Minimize the risk by having a smooth cost of capital and value of the firm.
- Issuance of shares is only made when the share market price is consistent and according to the firm's objective.
- Increasing trends obtain high revenue and cash flows in the financial and non-financial markets when one's had a positive increment in stock price.
- The performance and value of the firm depend on share price and dividend policy also the financial behavior of themarkets.
- Economic indicators are also focused on when a firm adopts different approaches.

Future Research

This study offers analysis for financial, non-financial, commercial, insurance, mutual funds and other sectors listed in the emerging Stock Exchange in which the most important extreme is taken which is share market price and its impact on corporate dividend policy. Consistency and volatility are found among variables in the financial and non-financial markets of the economy which help them at the time of investment and taking rational decisions.

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