International Journal of Advanced Research in Commerce, Management & Social Science (IJARCMSS)
ISSN : 2581-7930, Impact Factor : 5.880 , Volume 04, No. 01, January - March, 2021, pp 133-137

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

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**ABSTRACT**

*The aim of this study is to examine the impact of dividend decisions on share prices of the selected pharmaceutical companies listed on the Bombay Stock Exchange. The research is completely based on secondary data. 15 pharmaceutical companies who have regularly paid dividend during the last five years have founded the sample of the study. The data regarding the average share prices is collected for 10 days before and 10 days after the declaration of dividend by the companies. T-test for paired sample means is used for examines the impact of dividend decision on the average share prices of the selected pharmaceutical companies. The outcome of the study shows that the share prices of the companies are not affected by the dividend announcement. It means that the shareholders' wealth is irrelevance hypothesis to the dividend declaration in the case of selected pharmaceutical companies firms listed on the Bombay Stock Exchange.*

***Keywords:*** *Dividend, Pharmaceutical Companies, Share Prices, Bombay Stock Exchange.*

## Introduction

The investment landscape can be really dynamic and ever-evolving. But those who take the time to understand the simple principles and the different asset classes stand to gain significantly over the long haul. Most investors want to make investments in such a way that they get very high returns as quickly as possible without the risk of misplacing principal money. This is the reason why many are continuously on the lookout for top investment plans where they can double their money in few months or years with little or no risk. Thus, the investor attempts to trade-off between risk and return. Dividend attracts the stakeholders to invest in shares.

Dividend is the indicator of financial position, wealth of the business, management efficiency and overall performance of the firm. Management should take care of the expectations of the stockholders while formulating dividend policy. Dividend policy determines the proportion of earnings to be distributed among stockholders as dividend and the proportion of earnings to be reinvested in the business. Dividend disbursement should be preferred if it results in the maximization of shareholders' wealth. If not, reinvestment is the well option. There are various opinions about the relationship between dividend and shareholders' wealth.

India enjoys an important position in the universal pharmaceuticals sector. The country also has a huge pool of scientists and engineers who have the potential to steer the industry ahead to an even higher level. India is the biggest supplier of generic drugs globally. Indian pharmaceutical sector industry supplies over 50 per cent of global demand for different vaccines, 40 per cent of generic demand in the US and 25 per cent of all medicine in UK.

Indian pharmaceutical sector is predictable to grow to US$ 100 billion and medical device market expected to grow US$ 25 billion by 2025. Pharmaceuticals exports from India stood at US$ 19.14 billion in FY19 and US$ 13.69 billion in FY20 (up to January 2020). Pharmaceutical exports include bulk medicines, intermediates, drug formulations, biological, Ayush& herbal products and surgical.India's biotechnology industry comprising biopharmaceuticals, bio-services, bio-agriculture, bio-industry and bioinformatics is predictable grow at an average growth rate of around 30 per cent a year and reach US$ 100 billion by 2025.

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**Review of Literature**

**Akram Budagaga** (2017) the researcher has studied on “Dividend Payment and its Impact on the Value of Firms Listed on Istanbul Stock Exchange: A Residual Income Approach.” In this paper, authors have empirically investigated the impact of dividend payments on the value of firms for a sample of 44 businesses listed on the ISE. The researcher founds that there is a significant positive relationship between cash dividends per share and a firm’s value.

**Merton H. Miller and Franco Modigliani** (1961), have done research on “Dividend Policy, Growth and the Valuation of Shares,” Journal of Business. The authors have found that the firms’ value depends on its earning capacity and not by its dividend paying policy. According to researchers dividend policy is an irrelevance for finding the true value of firms share price.

**Dr. Syed Zulfiqar Ali Shah, WasimUllah and Baqir Hasnain**(2011) have studied on “Impact of ownership structure on dividend policy of firm.” In this paper authors have investigated the dividend policy of the listed companies in perspective of ownership control. Results point out that managerial ownership appears to have a visible and significant effect on dividend pay-out.

**Kevin Campbell and Chijioke Ohuocha**(2011) have studied on “The Stock Market Reaction to Stock Dividends in Nigeria and their Information Content.” In this paper authors have concluded that companies that decide on their own announcement date outside the Nigerian stock exchange announcement window experience positive abnormal returns if their stock is more regularly traded and negative abnormal returns if their stock is less frequently traded.

**Joshi, A. & Mayur, M.** (2017) have studied the share price reactions of top 20 Public sector companies by market capitalization which were listed in Bombay Stock Exchange (BSE), covering 20 days of announcement during the period 2013-2016. The outcomes show that there was a significant difference on the prices of shares in before and after declaration of dividend of the selected companies.

**Hetal Tank** (2018) has conducted a study on “An impact of dividend decisions on share prices of the company: A study of selected pharmaceutical companies”. The researcher founds that the dividend declaration does not affect the average share prices of the firm. It means whether the company pays the dividend or not, it doesn’t make any difference on the average share prices of the selected pharmaceutical companies.

**Ahmed Butt Iftikhar, Nabeel-Ud-Din Jalal Raja and Khan Nisar Sehran** (2017) studied the “Impact of dividend policy on stock prices of firm”. The author concluded that dividend policy has a significant effect on firm’s performance and firm market value. The researchers have observed on the basis of results the firms should focus on dividend policy in terms of gaining trust and attention of the investors.

**Khushboo Vora** (2018) has examined the “Influence of financial performance indicators on market price of shares of Nifty 50 companies”. The researcher has observed that ROI and EPS have a strong, significant and positive impact on market share price. The author also concluded that, one can confirm that ROI and EPS have a noticeable impact on share price. ROA and ROE, if ever used, would be a weak negative predictor of market share price.

**Objectives of the Study**

The principal objective of the study is to analyze the impact of dividend decisions on share prices of the selected pharmaceutical companies in India listed on the Bombay Stock Exchange. To accomplish this objective following specific objectives have covered:

- To understand the dividend policy of the selected pharmaceutical companies in India.
- To analyze the impact of dividend declaration on the average share prices of selected pharmaceutical companies in India.

**Hypotheses of the Study**

**$H_0$:** There is no significant difference between the average share prices of selected pharmaceutical companies 10 days before and 10 days after declaring dividend.

**$H_1$:** There is a significant difference between the average share prices of selected pharmaceutical companies 10 days before and 10 days after declaring dividend.

**Research Methodology**

**Sources of Data**

This study is totally based on the secondary data and the data is collected from the official website of BSE (www.bseindia.com). Many articles and research papers are also reviewed for the better understanding of the subject problem of the study.

**Period of the Study**

The study covers the period of one year starting from 1st April, 2019 to 31st March 2020. The data related to average share prices of selected pharmaceutical companies 10 days before and 10 days after declaring dividend are considered for the study.

**Sampling Design**

15 pharmaceutical companies are selected as a sample for the present study. The pharmaceutical companies who are listed on Bombay Stock Exchange and who have declared the dividend regularly during the last 5 years (2015-16 to 2019-20) are selected as a sample of the study. The list of such companies is as follows:

**Table 1**

| Sr. No | Name of the Pharmaceutical Companies |
|---|---|
| 1. | Sun Pharmaceutical Industries Limited |
| 2. | Dr Reddys Laboratories Limited |
| 3. | Divis Laboratories Limited |
| 4. | Cipla Limited |
| 5. | Lupin Limited |
| 6. | Torrent Pharmaceuticals Limited |
| 7. | Cadila Healthcare Limited |
| 8. | Alkem Laboratories Limited |
| 9. | GlaxoSmithKline Pharmaceuticals Limited |
| 10. | Ipca Laboratories Limited |
| 11. | Sanofi India Limited |
| 12. | Alembic Pharmaceuticals Limited |
| 13. | GlenmarkPharma Limited |
| 14. | Ajanta Pharma Limited |
| 15. | Jubilant Life Sciences Limited |

**Statistical Tools and Techniques**

T-test: Paired two samples for means is used to observe the impact of dividend declaration on the share prices of selected pharmaceuticalcompanies in India.

Here, $\text{Average Share Price} = \frac{\textbf{Opening share Price} + \textbf{Closing Share Price}}{\textbf{2}}$

**Significance of the Study**

The result of the study is useful to following parties:

- This study provides valuable information to investors related to possible changes in share prices due to dividend declaration.
- It also supports financial managers and financial advisors in formulating dividend policy.

**Limitation of the Study**

The following are the limitations of this study:

- As the study conducted only for 15 pharmaceutical companies, the generalization of results cannot be made for complete industry.
- The present study is totally based on secondary data. So, the limitations of using secondary data are also present in the study.

**Theories of Dividend given by Various Authors**

There are mostly three well known theories of dividend policy which are defined as below:

- **Modigliani and Miller Hypothesis of Dividend Irrelevance**

Franco Modigliani and Merton H. Miller have advocated that, the dividend strategy of a firm is irrelevant, because it does not affect the value of the shareholders. It means that the value of the firm is self-regulating of its dividend policy. Worth of the firm is dependent on the firm’s earning capacity, which results from the investment strategy of the company and not from the dividend policy of the company. It means that for the determination of the value of firm, dividend decision is not a suitable tool.

- **Gordon's Model of Dividend Relevance**

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

- **Walter's Model of Dividend Relevance**

James E. Walter has given the model of dividend theory in 1963, which describes that for determination of value of shareholders, dividend decision is important factor. Investment decision and dividend decision are interlinked with each other. According to Walter, investment decision and dividend decision cannot be divided. If the company pays dividend, then the stockholders reinvest the same, to get higher returns. This is well-known as opportunity cost or cost of capital for the firm. If the company does not pay out the dividends and retains earnings in moneymaking opportunities to earn returns. Thus, the rate of return for the firm must at least be the same to cost of capital.

**Analysis using T-Test: Paired Two Sample Means**

The following table shows the average share prices of selected pharmaceutical companies before and after 10 days of dividend declaration.

**Average Share Prices of Selected Pharmaceutical Companies**

**(Before and After Dividend Declaration)**

**Table 2**

| Sr. No. | Name of the Companies | Before | After |
|---|---|---|---|
| 1 | Sun Pharmaceutical Industries Limited | 414.61 | 412.66 |
| 2 | Dr Reddys Laboratories Limited | 2858.99 | 2661.43 |
| 3 | Divis Laboratories Limited | 1689.05 | 1596.20 |
| 4 | Cipla Limited | 554.15 | 568.51 |
| 5 | Lupin Limited | 846.49 | 761.49 |
| 6 | Torrent Pharmaceuticals Limited | 1657.46 | 1548.98 |
| 7 | Cadila Healthcare Limited | 252.33 | 252.51 |
| 8 | Alkem Laboratories Limited | 1704.33 | 1777.75 |
| 9 | GlaxoSmithKline Pharmaceuticals Limited | 1274.16 | 1276.04 |
| 10 | Ipca Laboratories Limited | 925.62 | 934.93 |
| 11 | Sanofi India Limited | 7237.05 | 7383.22 |
| 12 | Alembic Pharmaceuticals Limited | 552.88 | 533.40 |
| 13 | GlenmarkPharma Limited | 571.48 | 541.93 |
| 14 | Ajanta Pharma Limited | 972.24 | 1017.26 |
| 15 | Jubilant Life Sciences Limited | 615.30 | 538.65 |

The following results are found for the selected pharmaceutical companies by applying t-test:

**t-Test: Paired Two Sample for Means**

**Table 3**

| Particulars | Before | After |
|---|---|---|
| Mean | 1475.07 | 1453.66 |
| Variance | 3007955.48 | 3110593.97 |
| Observations | 15 | 15 |
| Pearson Correlation | 1.00 | -- |
| Hypothesized Mean Difference | 0 | -- |
| df | 14 | -- |
| t Stat | 1.00 | -- |
| P(T<=t) one-tail | 0.17 | -- |
| t Critical one-tail | 1.76 | -- |
| P(T<=t) two-tail | 0.33 | -- |
| t Critical two-tail | 2.14 | -- |

**Statistical Analysis & Findings**

- Since the value of 't' in the table at 5% level of significance and with degree of freedom n-1 = 14, is more than the calculated value in case of average share prices of the selected Pharmaceutical Companies in India declaring dividends, therefore the Ho is significant and accepted.
- Hence, we can say that there is no significance difference between the average share prices of selected 15 pharmaceutical companies before 10 days and after 10 days of declaring dividend.
- It means that share prices of the selected pharmaceutical companies are independent from the firm's dividend decision.
- The outcome of the present study is supported by Modigliani and Miller Hypothesis of Dividend Irrelevance theory. According to this concept, the share prices of the firm are independent from its dividend decision.
- The MM method is based on the operation of arbitrage. It means if the company retains earning, then the shareholders enjoy capital appreciation which is the same to the amount of retained earnings. If the company pays out the dividend, then the stockholders enjoy dividend which is equal to the value of capital rise. Thus, the dividend decision is irrelevant for the determination of stockholders' wealth.
- Two companies who have same amount and same type of risk, having same future potential of earnings and same investment strategies will have the same market price of the shares, irrespective of their dividend decisions.

**Conclusion**

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

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