

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Dividend policy is the major decision of the firm. Mostly, dividend is paid in cash to its shareholders. Dividend payment reduces the total amount of internal financing. Consequently, it must be considered in relation to the overall financial decision. “A commercial bank is a dealer of money and substitute for money, such as check or a bill of exchange. It also provides a variety of financial services” (The Encyclopedia of Britannic; 1985: 600).

“Ordinary banking business consists of changing cash for bank deposit and bank deposit for cash transactions, bank deposit from one person to corporations dividing bank deposit in exchange for the bills of businessmen to repay” (Gupta; 1984:15).

“A joint venture is the joining of forces between two or more enterprises for the purpose of carrying a specific operation, industrial or commercial investment, production or trade” (Gupta; 1984: 15).

In the global perspective, joint ventures are the modes of trading through partnership among nations and also a form of negotiation between various groups of industries and traders to achieve mutual exchange of goods and services for sharing competitive advantages.

“By a dividend policy, we mean some kind of consistent approach to the distribution versus retention decision rather than making the decision on purely ad-hoc basis from period to period” (Pearson,Charles and Gordon; 1972: 405). The dividend payout ratio obviously depends on the way earnings are measured but net earning may not confirm and may not be an approximate measure of the ability of the firm to pay dividend. So, what and how much it is desirable to

pay dividend is always a controversial topic because shareholders expect higher dividend.

“The issue, of how much a company should pay its stakeholders as dividends, has concerned managers for a long time now. It has often been pointed out that a company that raises its dividends often experiences an increase in its stock price and that a company that lowers its dividends has a falling stock price. This seems to suggest that dividends do matter, in that they affect stock price. But this casual relationship has been refuted by several researches on the grounds that dividend per share does not affect stock prices, rather it is the informational content of dividend that affect stock prices”(Rao; 1992: 448).

There are again corporate laws that bind limitation on the distribution of dividend, as corporation has to keep reserves for the protection of creditors overall interests. It is there a wise policy to maintain balance between shareholders’ interest with that of corporate growth from internally generated funds. The return to shareholders should be better paid as dividends, since shareholders have investment opportunities to employ elsewhere.

“The objective of a dividend policy should be to maximize shareholders’ return so that the value of their investment is maximized. Shareholders’ return consists of two components: dividend and capital gain. Dividend policy has direct influence on these two components of return” (Pandey; 1999: 744).

In a capital structure decision, each and every firm can obtain additional fund by issuing new equity and retention of the earnings. So, after measuring the firm’s profit, there is further problem of what amount of these profits should be distributed in terms of dividend. It is a big financial decision because the firm has to choose one between the distribution of profit to the shareholders or retaining it to finance the business. Different firms adopt different approaches to distribute dividend. In order to maximize the shareholders’ wealth, the firm should use a large amount of profit for the payment of dividend. But since the

firm's objective is the expansion of its business, the firm retains profit to finance in investment programs.

Dividends are distributed out of profits. The alternative to the payment of dividend is the retention of earnings/profits. The retained earnings constitute an easily accessible important source of financing the investment requirement of firms. There is, thus, a type of reciprocal relationship between retained earnings and cash dividends. The larger the retention, the lesser the dividend; the smaller the retention, the larger the dividends. Thus, the alternative uses of net earning –dividend and retained earning are competitive and conflicting (Khan and Jain; 1990:35).

Having given the overall dividend implication among companies and financial institutions, this study is more specific in assessing the dividend practices of the commercial banks especially Bank of Kathmandu and Everest Bank Ltd.

1.1.1 History of Banks in Nepal

Talking about the history of bank, an institutional banking system came into existence in Nepal only in the 19th century. Nepal Bank Limited was the first financial institutional of Nepal established on the 30th of Kartik 1994. Being a commercial bank, it focuses on income generating and profit maximization. As it was only one commercial bank, it has to look the economic condition of country. Only one Nepal Bank Limited was not sufficient to look all the sector of country. So in 2013 B.S. another bank named “Nepal Rastra Bank” was established as the central bank. Similarly the 2nd commercial bank Rastriya Banijya Bank was established as the second commercial bank of Nepal in Magh 10, 2022 B.S., under Rastriya Banijya Bank Act 2021. This act is now revised as Commercial Bank Act 2031. B.S. “Accepting deposits, granting loan and performing commercial banking functions are the main motto of commercial bank” (Commercial Bank Act, 2031). For the development of industry, commerce and trade, Nepal Industrial Development Corporation was established under Industrial Development Corporation Act 2016. For the

development of agricultural section, Agricultural Development Bank was established on Magh 7th 2024 B.S., under the Agricultural Bank Act 2024 B.S.

The government of Nepal observed the necessities of rapid development of the country for which it has adopted “liberalized economic policy, laissez fair economy and encouraged foreign investment”. “The government formed Foreign Investment & Technology Act 1981 A.D. which was later revised as Act 1992 A.D. by new elected democratic government”(Foreign Investment and Technology Act, 1992). The joint venture bank was introduced in Nepal in 2041 B.S. with the establishment of “Nepal Arab Bank Limited”. It was established with joint venture of U.A.E bank, financial institution of Nepal.

The second joint venture bank, Nepal Indosuez Bank Limited was established in 6th Magh 2042 B.S. Similarly, others joint venture banks like, Nepal Grindlays Bank Limited on 16th Marg 2043, Himalayan Bank Limited on 2049 B.S., Nepal State Bank of India Limited on 2050 B.S., Nepal Bangladesh Bank Limited on 2051 B.S., Everest Bank Limited on 2051 B.S., Bank of Kathmandu on 2052 B.S. and Nepal Bank of Celon Limited on 2052 B.S. have been established. Till now other commercial banks have been also established.

Among them majority of banks are established in joint venture banks. “A joint venture is the joining of forces between two or more enterprises for the purpose of carrying out a specific operation industrial or commercial investment, production or trade” (Gupta, 1984: 15).

Joint venture banks play an important role for economic development of nation. They have been adopted new banking technique, management like, hypothecation, syndication lending polices, tale banking credit card, master card from international banking technique. They render various services to their customers in order to facilitate their economic and social life. Joint venture banks are operating in Nepal in an act as commercial banks are operating and performing their work under the direction of Nepal Rastra Bank. Nowadays, there are many joint venture banks and other financial institutions,

but there are little opportunities to make fair investment. Meanwhile, the banks and financial institutions are offering very low deposit and credit interest rate. So to survive in the competitive banking market, one should follow the fundamental principles of sound investment policy with minimum risk and maximum profit.

At present, about a dozen of the joint venture banks are operating in Nepal and are playing important role in the economic development of the country.

1.2 Statement of the Problem

Dividend, the most inspiring factor for the investment on shares of the corporation, is an important aspect of financial management. Because the dividend policy determines the division of earnings between payment to stockholders and reinvestment in the firm to exploit growth opportunities. It affects the value of firm as well as overall financing decision such as financial structure, the flow of funds, corporate liquidity and investors' satisfaction.

The dividend decision, however, is still a crucial as well as controversial area of managerial finance. There is no consensus among the financial scholars on this subject matter and its relation with stock price. Some financial scholars say that stock prices are least influenced by dividend per share while some others believe that its relevance to the stock prices is quite significant. The idea of relevance is vague as well. It is rather hard to define whether dividend per share has positive effect or its effect is negative one.

Dividend is desirable for the shareholders, which inspires them for the further investment on company's shares. But it is found that there is no satisfactory result about dividend decision of commercial banks in Nepal. Likewise, dividend distribution does not match with the earnings of the commercial banks, there does not exist a proper relationship between dividend and quoted market price of share. Similarly, commercial banks with lower returns record

stable (rigid) price of share and banks making sound returns do not rigid in share price.

It is because, among the various reasons, the government rules and regulations, ownership patterns, attitudes of management, forms of management may be the partial causes of such a situation. In practice, every firm follows some kinds of dividend policy and there is no unique dividend policy which is appropriate (suitable) for all the firms. So they follow different policies. In general, it is assumed that there is relationship between dividend and stock price but the relation in under developed country like Nepal is not yet known. So the relation between dividend and stock prices established by much finance scholars needs to be tested in the context of Nepal.

In the Nepalese context, the companies listed in NEPSE are not seen so serious regarding dividend decisions, since most of them do not have any consistent and obvious (clear cut) policy on dividend distribution. In connection to Nepalese public enterprises, M.K. Shrestha remarks that dividend is still considered as the unintended strategy or the non payable obligation at a time when Nepalese government is not in a position to impose the public limited companies to pay a minimum rate of dividend on the equity capital contributed. Some Nepalese acts like Nepal Company Act 2053, Nepal Commercial Bank Act 2031 and other regulating acts are still silent regarding dividend distribution. So different companies are adopting different dividend decisions inconsistently. There is a common trend of deciding the dividend by the management of companies instead of by shareholders meeting.

This study raises some issues to be examined which are stated below:

- (a) Whether the problem is attitude to pay dividend or the ability to pay dividend.
- (b) Whether there is uniformity of dividend distribution or not.
- (c) Whether dividend decision affects the market price of shares differently in different banks or not.

- (d) Whether or not the prevailing dividend policy influences the corporate liquidity position.
- (e) Whether changing dividend policy or payout ratio increase the value of stock or not.
- (f) What is the relationship between dividend with other key variables like earning per share, market price per share, book value per share, net profit and net worth of the banks?
- (g) What are the prevailing practices of the banks regarding their dividends?

1.3 Objectives of the Study

The objective of a dividend decision should be to maximize the shareholders' return so that the value of his investment is maximized. This study is primarily undertaken to focus on the prevalent dividend policies and to suggest the direction of future endeavors for the overall healthier development of the share market and also the possible impact of such endeavors on the share market in Nepal.

The main objectives of this study are as follows:

- a. To identify what type of dividend policy is being followed and whether or not the followed policy is appropriate in Bank of Kathmandu and Everest Bank Limited
- b. To highlight dividend practices of the Bank of Kathmandu and Everest Bank Limited.
- c. To analyze the relationship between dividend per share with various important variables such as earning per share, net profit, net worth and stock prices.
- d. To provide a practical suggestion and possible guidelines to overcome various issues and gaps based on the findings of the analysis.

1.4 Significance of the Study

Due to excess liquidity and lack of investment opportunities in the capital market, nowadays people are very much interested and attracted to invest in shares for getting higher returns. When any new company issues (floats) shares through capital markets, very big congregation gathers to apply for owner's certificate. It reveals that people have expectation on higher return for investing in shares. So the dividend decision is one of the most important decisions of financial management. It is an effective tool (way) to attract new investors, maintain present investors and controlling position of the firm. In capital market, basically, the return can be earned in the following two ways:

- (i) By means of dividend
- (ii) By capital gains i.e., increase in share price.

Having lack of adequate knowledge, the people are haphazardly investing in shares. It shows that there is an extreme necessity to establish clear conception about the return that yields from investing in securities.

In the Nepalese perspective, we find that there exist almost none of the companies adopting consistent dividend policy. There may be many reasons behind it. But there is not sufficient study conducted in this regard. So, I have made this humble attempt to contribute to this aspect. Therefore, considering all these facts, the study is undertaken which will help to meet deficiency of the literature relating to dividend decision and factors affecting the dividend policy. So the study of dividend policy is of considerable importance.

I believe that so many persons and parties such as shareholders, management of banks, financial institutions, general public (depositors, prospective customers, investors etc.) and other policy making bodies which are concerned with banking (especially Bank of Kathmandu and Everest Bank Ltd.) business will be benefited from this study. It is also believed that it will provide valuable inputs for future research scholars.

1.5 Limitations of the Study

There are limitations that weaken the generalizations – e.g. inadequate coverage of industries, shortage of time, reliability of statistical tools used and other variables. This study is simply a partial requirement of MBS program. So, this study will be limited by the following:

- a) The data collected depends upon the accuracy of the annual reports of banks.
- b) The study period only covers five fiscal years.
- c) Due to insufficiency of time, only two joint venture banks are taken as samples.
- e) There are many factors that affect dividend decisions and valuation of the firm. However, only those factors related with dividend will be considered in the study

1.6 Chapter Scheme

This study comprises of five chapters. Given below are the headings under which the entire study has been categorized:

Chapter 1 – Introduction

Chapter 2 – Review of Literature

Chapter 3 – Research Methodology

Chapter 4 – Data Presentation and Analysis

Chapter 5 – Summary, Conclusion and Recommendations

The first chapter deals with the subject matter consisting introduction, focus of the study, statement of the problem, objectives of the study, and significance of the study and chapter scheme of the study.

The second chapter deals with review of literature that includes the conceptual framework, factors influencing dividend policy, review of major studies, review of journals and articles in Nepalese perspective and review of theses.

The third chapter describes research methodology employed in the study. It includes introduction, research design, and sources of data, population and sample, method of analysis, tools defined about certain financial indicators and statistical tools used.

The fourth chapter deals with analysis of financial indicator variables, analysis of means, standard deviation, correlation matrix and simple regression analysis.

Lastly, the fifth chapter consists of main findings, issues and gaps, future guidelines alongside summary, conclusion and recommendations.

CHAPTER II

REVIEW OF LITERATURE

This research aims to analyze the dividend policy and practices of commercial banks especially two joint venture banks viz. Bank of Kathmandu Ltd. and Everest Bank Ltd. For this purpose, it is helpful to review related literatures in this concerned area which will help to get clear ideas, opinions and other concepts. 'What others have said? What others have done? And what others have written?' all these and other related questions are reviewed, which has provided useful inputs in this research work. This chapter emphasizes on the literatures which are concerned with this connection. Therefore, in this chapter, conceptual frameworks given by different authors and intellectuals on this area, books, journals, research works, and previous thesis related to dividend and dividend policies and practices are reviewed. Moreover, rules regarding to dividend policy are reviewed and an attempt has been made to present them properly.

2.1 Conceptual Framework

Dividend decision is an integral part of financial management decision. It is in the sense that the firm has to choose between distributing the profits to the shareholders and reinvesting it to finance the business. The important aspect of dividend policy is to determine the amount of earnings to be distributed to shareholders in return to their investment and the amount to be retained in the firm. It affects the financial structure, the flow of funds, corporate liquidity and investor's attitudes. It is a matter of interest for all the stakeholders. Thus, it is one of the central decision area related to policies seeking to maximize the value of firm's common stock.

Iqbal Mathur defines the dividend and dividend policy as: "Dividends refer to that portion of retained earnings that is paid to stockholders while dividend policy refers to the policy or guidelines that management uses in establishing

the portion of retained earnings that is to be paid in dividends” (Mathur; 1979: 297).

The policy of a company in the allocation of its profits between distribution to shareholders as dividend and retention for its investment is known as dividend policy. All aspects and questions related to payment of dividend are contained in a dividend policy. Generally, dividends are paid in the form of cash, which reduces the cash balance of the company. There is a reciprocal relationship between retained earnings and cash dividends. If retained earning is kept more by the company, less will be the dividend and vice - versa. The decision depends upon the objective of the management for capital maximization.

What and how much is desirable to pay dividend, is always a matter of dispute because shareholders expect higher dividend from company, as it tends to increase their current wealth whereas retention of earning is desirable for the growth of firm. These two objectives of the dividend policy are always in conflict. There is not yet consensus on whether the firms should follow certain pattern to distribute dividend and retain earnings. However, there is different decision models developed to analyze the situation and reach a decision. These decision models are conflicting and consider the different aspects of the firm. One school of thought argues that dividend payment has no impact on valuation of a firm whereas other theories of dividend decision argues dividend to be active variable in valuation of firm. These different models on the relationship between dividend and the value of the firm will be discussed later on in this chapter in detail.

2.1.1 Concept of Dividend

The various concepts of dividend, defined in various books of finance, are discussed below:

(a) Discretionary concept

When the board of directors declares the amount of dividend, it is known as discretionary dividend. According to this concept, dividend payment is one of directors' decisions and so they use discretion in declaration of dividend. Corporations' charter vested powers to board of directors and it is up to their discretion that determines what and how much to pay by way of dividends to stockholders.

"The power to declare dividends is lodged in the board of directors of the corporation. At a meeting of the board, in accordance with the charter and corporate by-laws, the board passes a resolution declaring the amount of dividend, the period which it covers, the payable date, and the record date of ownership" (Cooke and Bomeli; 1967:180).

Even in the context of Nepalese corporations, the decision regarding the payment of dividend is purely vested in the board of directors of corporation, and it is also insisted by the corporate acts. There are not any legal rights to demand any part of profit in the form of dividends by the ordinary shareholders because profits are the property of the corporations and not of individual shareholders.

(b) Pro-Rata distribution concept

"A dividend is a pro-rata distribution of cash, other assets, promises to pay, or additional stock to the shareholders of a corporation chargeable against its surplus accounts or (for certain liquidating dividends only) against its capital stock accounts" (Cooke and Bomeli; 1967:180).

The pro-rata distribution refers to proportionate share of all outstanding stock, or all shares of a given class, which participate equally in whatever is distributed. Thus, under this concept, all shareholders enjoy equal right on the profit distributed by the corporations, according to their proportion of shares.

(c) Residual concept

“Dividend is the residue left after meeting all obligations and adjusting for retention of earnings and other provisions. It is a residue since shareholders get dividends only when there exists balance of earnings after paying fixed obligations such as operating expenses, interest, provisions for depreciation, and setting”(Van Horne;1993 : 327).

Under this concept, dividend policy is a residual firm investment policy and dividends are paid only after financing all investment opportunities. So, dividend policy is totally passive in nature. "When we treat dividend policy as strictly a financing decision, the payment of cash dividends is a passive residual"(Van Horne; 1993: 327).

(d) Liability Concept

Dividend once declared by the board of directors, becomes a liability of the corporation. "When the board of directors of a solvent corporation declares cash dividend, the amount declared becomes an obligation to pay." If the directors avoid payment of dividend after declaration, the shareholders would have a right to take action against the directors to force payment. The dividends declared are treated as liabilities in the balance sheet if the shareholders do not come to claim in time.

2.1.2 Conflicting Theories on Dividends

Basically, there are two schools of thoughts on dividend policy which have been expressed in the theoretical literature of finance. One school, associated with Myron Gordon and John Lintner, holds the view that capital gains expected to result from earnings retention are riskier than are dividend expectations. In other words, dividend yield is less risky than the expected capital gain. It also says that investors give more emphasis to the present dividend than future capital gain. Investors are not indifferent between current dividend and retention of earnings with the prospects of future dividends, capital gain and both. Accordingly, these theorists suggest that the earnings of a

firm with a low payout ratio are typically capitalized at higher rates than the earnings of a high payout firm, other things held constant.

Another school of thought, associated with Merton Miller and Franco Modigliani, holds the view that investors are basically indifferent to returns in the form of current dividends or retention of earnings with the prospects of future dividends, capital gain. When firms raise or lower the dividends, their stock prices tend to rise or fall in like manner. They argue that, given the investment decision of the firm, the value of firm is determined safely by the firms earning power and that the manner in which the earnings split between dividends and retained earnings does not affect the value of firm. In other words, when investment decision of the firm is given, dividend decision, the split of earnings between dividends and retained earnings, is of no significance in determining the value of firm.

2.1.3 Types of Dividend

Though cash dividend is assumed to be the most popular form of dividend, corporation needs to follow various types of dividend according to the objectives and policies, which they implement. "The type of dividend that corporations follow is partly a matter of attitude of directors and partly a matter of the various circumstances and financial constraints that bound corporate plans and policies " (Shrestha; 1980:670).

According to the changing needs of corporations, dividend is being distributed in several forms viz. cash dividend, stock dividend (bonus share issue), scrip dividend, property dividend, optional dividend and bond dividend. But in Nepal and India only two types of dividend namely cash dividend and stock dividend are being practiced.

i. Cash Dividend

Cash dividend is the form of dividend, which is distributed to shareholders in cash out of earnings of company. The cash account and the reserves account of

a company will be reduced when the cash dividend is paid. Thus, both the total assets and the net worth of the company are reduced when the cash dividend is distributed. The market price of the share drops in most cases by the amount of the cash dividend distributed. (Hastings; 1996:370)

So the companies should wisely make decisions regarding payment of cash dividend.

ii. Stock Dividend / Bonus Share

A stock dividend represents the distribution of shares in addition to the cash dividend to the existing shareholders. This has the effect of increment in the number of outstanding shares of the company. The declaration of the bonus shares will increase the paid-up share capital and reduce the reserve and surplus of the company. The total net worth is not affected by the bonus issue. In fact, it represents nothing more than re-capitalization of the owners' equity portion, i.e., the reserve and surplus. It is simply an accounting transfer from retained earning to capital stock.

iii. Scrip Dividend

A scrip dividend is issued when company has been suffering from the cash problem and does not permit the cash dividend, but has earned profit. A dividend paid in promissory notes is called a scrip dividend. Scrip is a form of promissory notes promising to pay the holder at specified later date. Under this form of dividend, company issues and distributes transferable promissory notes to shareholders, which may be interest bearing or non - interest bearing. The use of scrip dividends is desirable only when corporations have really earned profit and have only to wait for the conversion of other current assets into cash. Therefore, in order to overcome the temporary shortage of cash, sometimes company uses scrip dividends.

iv. Property Dividend

It is also known by the name of liquidating dividends. It involves a payment of assets / property in any form other than cash. Such form of dividend may be

followed whenever there are assets that are no longer necessary in the operation of the business or in extra ordinary circumstances. Companies own products and the securities of subsidiaries are the examples that have been paid as property dividend.

v. Optional Dividend

The optional dividend is, in fact, not a kind of dividend but simply a choice of dividend given to the shareholders to accept either cash or stock dividend. But the shareholders consider the comparative value of stock dividend with the amount of optional cash. "If the two are very nearly the same, as it often the case, the cash option may be a convenience to the small shareholder, who thus avoids the case and expense of selling either whole or fraction of shares he does not wish to keep" (Waring; 1931: 404).

If the cash dividend is subject to income taxes over and above the limit he prefers to have stock dividend.

vi. Bond Dividend

This type of dividend is distributed to the shareholders in the form of bond. It helps to postpone the payment of cash. In other words, company declares dividend in the form of its own bond with a view to avoid cash outflows. They are issued rarely. They are long term enough to fall beyond the current liability group. The stockholders become secured creditors if the bond carries lien on assets.

But none of these types except cash and stock dividend have been practiced in Nepalese corporations although they have ample scope for application. So far in this study, the term dividend generally refers to cash dividend.

2.1.4 Theories of Dividend

2.1.4.1 Residual Theory of Dividends

"The residual dividend policy suggests that dividend paid by the firm should be viewed as a residual amount left after all acceptable investment opportunities have been undertaken" (Lawrance; 1994: 537.17).

According to this theory, dividend policy is a firm's policy in which dividend is paid only after all acceptable investments have been financed. So, payment of dividend depends on its investment policy. In other words, the firms use earnings to finance the investment opportunities having good returns. If the firm has earnings left after financing all acceptable investment opportunities these earnings would then be distributed to shareholders in the form of dividend. If not, there would be no dividends. It assumes that the internally generated funds (i.e. retained earnings) are comparatively cheaper than the funds obtained from external sources (i.e. issuing new shares). It is because the retained earning or internally generated fund does not imply any flotation cost as in the external sources by selling equity shares.

So, under this theory, dividend policy is determined by the following two major factors:

- (i) Company's investment opportunities.
- (ii) Availability of internally generated funds i.e., retained earnings.

According to this concept, dividend policy is totally passive in nature. 'When we treat dividend policy as strictly a financing decision, the payment of cash dividend is a passive residual' (Van Horne; 1993:327).

2.1.4.2 Stability of dividends

Stability of dividends means regularity in paying some dividend annually, even though the amount of dividend may fluctuate from year to year and may not be related with earnings.

Stability or regularity of dividends is considered as a desirable policy by the management of most companies. Shareholders also generally prefer stable dividends because all other things being the same, stable dividends may have a positive impact on the market price of the share.

By stability, we mean maintaining its position in relation to a dividend trend line, preferably one that is upward slopping. In other words, the term dividend stability refers to the consistency or lack of variability in the stream of dividends. Precisely, it means that a certain minimum amount of dividend is paid out.

Three distinct forms of such stability may be distinguished.

1. Constant dividend per share

According to this form of stable dividend policy, a company follows a policy of paying a certain fixed amount per share as dividend. The fixed dividend amount would be paid year after year, irrespective of fluctuation in the earnings. In other words, fluctuations in earnings would not affect the dividend payment. In fact, when a company follows such a dividend policy it will pay dividends to the shareholders even when it suffers loss. It should be clearly noted that this policy does not imply that the dividend per share or dividend rate will never be increase. The dividend per share is increased over the years when the company reaches new levels of earnings and expects to maintain it. Of course, if the increase is expected to be temporary, the annual dividend per share is not changed and remains at the existing level.

It is easy to follow this policy when earnings are stable. If the earning pattern of a company shows wide fluctuations, it is difficult to maintain such policy. Investors who have dividends as the only source of their income prefer the constant dividend policy.

2. Constant Payout Ratio

Constant / target payout ratio is a form of stable dividend policy followed by some companies. The term payout ratio refers to the ratio of dividend to earnings or the percentage share of earnings used to pay dividend. With constant / target payout ratio, a firm pays a constant percentage of net earnings as dividend to the shareholders. In other words, a stable dividend payout ratio implies that the percentage of earnings paid out each year is fixed. Accordingly, amount of dividend will fluctuate in direct proportion to earnings and are likely to be highly volatile in the wake of wide fluctuations in the earnings of the company.

This policy is related to a company's ability to pay dividends. If the company incurs loss, no dividends shall be paid regardless of the desires of shareholders. Internal financing with retained earnings is automatic when this policy is followed. At any given payout ratio the amount of dividends and the additions to retained earnings increase with increasing earnings and decrease with decreasing earnings. This policy simplifies the dividend decision, and has the advantage of protecting a company against over and under payment of dividend. It ensures that dividends are paid when profits are earned, and avoided when it incurs loss.

3. Stable rupee dividend plus extra dividend (low regular dividend plus extras)

A policy of paying a low regular dividend plus a year end extra amount in good years is a compromise between the previous two policies. Under this policy, a firm usually pays fixed dividend to the shareholders and in years of marked prosperity, additional or extra dividend is paid over and above the regular dividend. As normal conditions return, the firm cuts the extra dividend and pays the normal dividend per share.

It gives the firm flexibility, but it leaves investors with somewhat uncertainty about what their dividend income will be. If a firm's earnings and cash flows are quite volatile, this policy might be the best choice.

2.1.5 Factors influencing dividend policy

Dividend policy, one of the major decisions of managerial finance, determines that what percentage of the earnings of the firm is distributed to its shareholders and what percentage of the earnings is retained in the firm which is desirable for the growth of the firm. Dividends are desirable to its shareholders because it tends to increase their current wealth whereas retained earnings are desirable for the firm to exploit investment opportunities as the internal source of financing. So, in order to develop a long term dividend policy, the directors should aim at bringing a balance between the desire of shareholders and the needs of the company. The firm's decision regarding the amount of earnings to be distributed as dividends depends on a number of factors. The factors which restrict the firm's ability to declare and pay dividends are discussed below:

(1) Legal Restrictions

(a) The surplus rule

According to surplus rule, dividend should be paid only out of profit. If there is no surplus or profits, dividend can't be legally declared.

(b) The insolvency rule

The insolvency rule states that dividends can't be paid if company is insolvent or if a payment would result in insolvency. (i.e when liabilities exceed assets.)

(c) Capital Impairment rule

According to this rule, dividend should not be paid if a firm's capital has been impaired or if dividend payment will cause capital to become impaired. It means dividends should not be paid out of paid - up capital.

(2) Bond Indenture

Debt contracts generally restrict dividend payments to earning generated after the loan is granted. Also, debt contracts often stipulate that no dividends can be paid unless the current ratio, the times interest-earned ratio and other safety ratios exceed stated minimums.

(3) Possibility of accelerating or delaying projects

The ability to accelerate or postpone project will permit more flexibility in a firm's dividend policy.

(4) Alternative sources of capital

(i) Cost of selling new stock

If a firm needs to finance a given level of investment, it can obtain equity by retaining earnings or by selling new common stock. If flotation costs are high, it is better to finance through retention than through sale of new common stock. On the other hand, if these costs are low, dividend policy will be less important. Flotation costs differ among firms. For example, they are generally higher for small firms. Hence, the importance of these costs, and consequently, the degree of flexibility in setting a dividend policy, varies among firms.

(ii) Ability to substitute debt for equity

A firm can finance a given level of investment with either debt or equity. As we have seen, if flotation costs are low, a more flexible dividend policy may be followed because equity can be raised by retaining earnings or by selling new stock. A similar situation holds for debt policy. If the firm is willing to adjust its debt ratio, it can maintain a constant amount of dividend by using a variable debt ratio.

(5) Need to repay debt

When a firm has sold debt to finance expansion or to substitute for other forms of financing, it is faced with two alternatives. It can refund the debt at maturity by replacing it with another form of security, or it can make provisions for paying off the debt. If the decision is to retire the debt, this will generally require for retention of earnings.

(6) Access to the capital market

All the firms do not have equal access to capital markets. A firm which has not sufficient liquidity can pay dividends, if it is able to raise debt or equity in the capital market. A firm which is larger, well established and has a record of

profitability will not find much difficulty in rising of funds in the capital market. Easy accessibility to the capital market provides flexibility to the management in paying dividends as well as in meeting the corporate obligations.

(7) Rate of assets expansion

The more rapid the rate at which the firm is growing, the greater is its need for financing assets expansion. The greater the future need for funds, the more likely the firm is to retain earnings rather than pay them out. If a firm seeks to raise funds externally, natural sources are the present shareholders, who already know the company. But if earnings are paid out as dividend and are subjected to high personal income tax rates, only a portion of them will be available for reinvestment.

(8) Internal investment opportunity

It is apparent that opportunities to invest are major consideration in setting dividend policy. Putting other considerations aside, when the firm has opportunities to earn returns greater than those available to shareholders outside the firm, retention and reinvestment are appropriate.

(9) Financial needs of the company

It is another consideration which also influences on the establishment of an appropriate dividend policy. Mature companies that have few investment opportunities may generally have high payout ratios. On the other hand, growth companies may have low payout ratios. They are continuously in need of funds to finance their fast growing fixed assets. The distribution of earnings will reduce the funds of the company.

(10) Profit rate

The rate of return on assets determines the relative attractiveness of paying out earnings in the form of dividends to stockholders who will use them in the current enterprise or some elsewhere.

(11) Tax position of the corporations

It is a factor which affects the firm's dividend decision. Possible penalties for excess accumulation of retained earnings may induce higher payout ratios.

(12) Stockholders' expectations

In case of widely-held company, the number of shareholders is very large and they may have conflicting interests and diverse desires regarding dividends and capital gains. Therefore, it is not easy to reconcile these conflicting interests of the various shareholders group by adopting a dividend policy which equally satisfies all shareholders.

Generally, the company should adopt a dividend policy which serves the purpose of the dominating group. But, it does not totally neglect the desires of other groups.

In a closely- held company, the body of shareholders is small and homogeneous group, so management usually knows the expectations of its shareholders and may adopt a dividend policy, which satisfies all shareholders. If most of the stockholders are in high tax brackets and have a preference for capital gains to current dividend incomes the company can establish a low dividend payout or no dividends and retains the earnings within the company.

(13) Tax of stockholders

The tax position of the corporation's owners greatly influences the desire for dividends. For example, a corporation closely held by a few taxpayers in high income tax brackets is likely to pay a relatively low dividend. The owners are interested in taking their income in the form of capital gains rather than as dividends which are subject to higher personal income tax rates. However, the stockholders of a large widely held corporation may be interested in a high dividend payout.

(14) Stability of earnings

A firm that has relatively stable earnings is often able to predict approximately what its future earnings will be. Such a firm is therefore more likely to payout a higher percentage of its earnings than is a firm with fluctuating earnings. The unstable firm is not certain that in subsequent years the hope for earnings will be realized, so it is likely to retain a high proportion of current earnings. A lower dividend will be easier to maintain if earnings fall off in the future.

(15) Control

The objective of maintaining control over the company by the existing management group or the body of shareholders can be an important variable in influencing the company's dividend policy. When a company pays large dividends, its cash position is affected. As a result, the company will have to issue new shares to raise funds to finance its investment programmes. The control of the existing shareholders will be diluted if they don't want or can't buy additional shares. Under this circumstance, the payment of dividends may be withheld and earnings may be retained to finance the firm's investment opportunities.

(16) Liquidity

The liquidity of a company is a prime consideration in many dividends decision. Although a firm may have sufficient retained earnings to declare dividend, but if they are invested in physical assets cash may not be available to make dividend payments. Thus the company must have adequate cash available as well as retained earning to pay dividends.

As dividends represent cash outflow, the greater the cash position and overall liquidity of a company, the greater is its ability to pay dividend and vice-versa. A company that is growing and profitable may not be liquidated, for its funds may go into fixed assets and permanent current assets.

(17) Inflation

In an indirect way inflation costs act as a constraint on paying dividends. Our accounting system is based on historical costs. Depreciation is charged on the basis of original costs at which assets were acquired. As a result, with raising prices funds saved on account of depreciation may be inadequate to replace obsolete equipment. Those firms have to rely upon retained earnings as a source of funds to make up the shortfall. This aspect becomes more important if the assets are to be replaced in the near future. Consequently, their dividend payment tends to be low during periods of inflation.

2.1.6 Legal provisions regarding dividend practices

There are no clear-cut legal provisions regarding dividend policy in Nepal. The responsibility to undertake required actions to protect shareholder's interest is given to Nepal Stock Exchange which is stated on the Security Exchange Act 1983. But this organization has not been so able to protect shareholders interest since interest and attitude of the board of directors play dominant role in management of public limited companies and they are generally in majority who are nominated by government.

According to Corporation Act, corporations must set aside a certain part of profit as reserves before the declaration of dividend. Moreover, corporations have to separate the tax provisions prior to dividend declaration.

Likewise, Commercial Bank Act 2031 has also made some provisions for distributing dividend. Section 18 of this act states about the restrictions for dividend distribution. According to this section, before providing the whole expenses by the bank for preliminary expenses, loss incurred in last year, capital reserve, risk beard fund reserve fund, the bank shall not declare and distribute the dividend to shareholders.

Similarly, Company Act 1997 makes some legal provisions regarding dividend distributions, which are discussed below.

According to this act, board of directors can fix dividend payout rate but such rate should be proposed ,first for the discussion and approval in the annual general meeting of shareholders, the general meeting can reduce the rate determined by board of directors but can't increase. Likewise, some other legal provisions are:

Section (2) (m) states that bonus shares mean shares issued in the form of additional shares to shareholders by capitalizing the surplus from the profits on the reserve fund of a company. The term also denotes an increase in the paid up values of the shares after capitalizing surplus or reserve funds.

Section (47) has prohibited company from purchasing its own shares. This section states that no company shall purchase its own shares or supply loans against the security of its own shares.

Section (137) bonus shares and sub-section (1) states that the company must inform the office before issuing bonus shares under sub-section (1); this may be done only according to a special resolution passed by the general meeting.

Section (140): Dividends and sub-sections of this section are as follows:

- (1) Except in the following circumstances, dividend shall be distributed among the shareholders within 45 days from the date of decision to distribute them.
 - (a) In case any law forbids, the distribution of dividends.
 - (b) In case the right to dividend is disputed.
 - (c) In case dividends can't be distributed within the time limit mentioned above owing to circumstances beyond anyone's control and without any fault on the part of the company.

(2) In case dividends are not distributed within the time limit mentioned in sub-section (1), this shall be done by adding interest at the prescribed rate.

(3) Only the person whose name stands registered in the register of existing shareholders at the time of declaring the dividend shall be entitled to it.

The above indicates that Nepalese law prohibits repurchase of stock, which is against the theory of finance. But the reason for this kind of provision is still unknown.

Similarly, followings are decisions regarding dividend payment by the government corporations dated June 14, 1998.

(1) Dividend should be paid in profitable years. Even though there are cumulative losses, dividend is to be paid if cash flow is sufficient to distribute dividend.

(2) In case of un-audited accounts, interim dividend should be paid on the basis of provisional financial statement.

(3) Dividend rate will not be less than the interest rate on fixed deposit of commercial bank of government owned. In case of insufficiency of profit amount to distribute dividend in above mentioned rate, concerned corporation should send proposal of new distribution rate to the Finance Ministry through liaison ministry and should do what so ever decision is given there of.

(4) Those corporations operating in monopoly situation should repay all amounts of profits to the government except the amount of bonus, tax and the amount needed to expand and develop the business. The amount separated for the expansion and development of business will not be more than 20 percent of profit of the year and this amount will not be more than

total paid up capital. The amount so separated should all be paid as dividend if it is not used within 3 years.

(5) Decision regarding distribution of annual net profit shall not be made without prior acceptance of Finance Ministry. All incentives, except those to be paid by law, shall not be distributed unless the amount of dividend is not paid to government.

(6) Concerned BOD and top management will be held responsible for implementation of these dividend policies.

(7) Ministry of Finance will make necessary arrangements regarding fixation of dividend percentage coordinating all concerned corporations and ministries.

2.2 Review of Major Studies

In this section, an attempt has been made to review of the major studies concerning dividends and stock prices and management views on dividend policy.

2.2.1 Lintner's Study

Lintner(1956) conducted a study on corporate dividend policy in the American context . He investigated a partial adjustment model as he tested the dividend patterns of 28 companies. According to John Lintner's study, dividends are 'sticky' in the sense that they are slow to change and lag behind shifts in earnings by one, or more periods. According to J. Lintner, dividend is a function of earnings of that year, existing dividend rate, target payout ratio and speed of adjustment. The followings were the basic objectives of the study.

- I. To identify occasions when a change in dividends might well have been under active consideration even though no change was made.
- II. To determine the factors existing most actively into dividends.

He concluded that a major portion of a firm's dividend could be expressed in the following manner.

$$DIV_t^* = P EPS_t \text{-----} (1)$$

$$\text{and } \text{DIV}_t - \text{DIV}_{t-1} = a + b (\text{DIV}_t^* - \text{DIV}_{t-1}) + e_t \text{-----}(2)$$

Adding DIV_{t-1} on both sides of equation (2)

$$\text{DIV}_t = a + b \text{DIV}_t^* + (1-b) \text{DIV}_{t-1} + e_t \text{-----}(3)$$

Where,

DIV_t^* = Firm's desired payment

EPS_t = earnings

P = Targeted payout ratio

a = constant relating to dividend growth

b = adjustment factor relating to the previous period's dividend and new desired level of dividends where, $b < 1$.

The major findings of this study were as follows:

- I. Firms generally think in terms of proportion of earnings to be paid out.
- II. In order to modify the pattern of dividend, investment opportunities, liquidity position, funds flows are not considered.

Firms generally have target pay out ratios in view while determining change in dividend rate or dividend per share. (Lintner; 1956: 99-113, extracted from, "Katuwal; 2001:30-31")

2.2.2 Modigliani and Miller Study

Modigliani and Miller (1961) conducted a study on the irrelevance of dividend. This is popularly known as MM approach. It is sometimes termed as Dividend Irrelevance Model.

According to MM, dividend policy of a firm is irrelevant as it does not affect the wealth of the shareholders. They argue that the value of the firm depends on the earning power of the firm's assets or its investment policy. Thus, when the investment policy is given, the dividend decision - splitting the earnings into packages of retentions and dividends does not influence the value of equity

shares. In other words, the division of earnings between dividend and retained earning is irrelevant from shareholders viewpoint.

In general, the argument supporting the irrelevance of dividend valuation is that dividend policy of the firm is a part of its financing decisions. As a part of the financing decision of the firm, the dividend policy of the firm is a residual decision and dividends are passive residual.

The MM approach of irrelevance dividend is based on the following critical assumptions:

- I. The firms operate in perfect capital market where all investors are rational. Information is freely available to all. Securities are infinitely divisible and no investor is large enough to influence the market price of securities.
- II. There are no flotation costs. The securities can be purchased and sold without payment of any commission or brokerage etc.
- III. Taxes do not exist.
- IV. The firm has a definite (fixed) investment policy, which is not subject to change.
- V. Risk of uncertainty does not exist. Investors are also able to forecast future prices and dividends with certainty, and one discount rate is appropriate for all securities and all time periods. Thus $r = k = kt$ for all time.

M-M provide the proof in support of their argument in the following manner.

Step-one

The market price of a share of the firm in the beginning the period is equal to the present value of dividends paid at the end of the period plus the market price of the share at the end of the period.

Symbolically,

$$P_0 = \frac{D_1 + P_1}{1 + K_e}$$

Where,

- $P_0 =$ Current market price of a share (market price at the beginning or at the Zero period.)
- $K_e =$ the cost of equity capital (Assumed constant)
- $D_1 =$ the dividend per share to be received at the end of the period one.
- $P_1 =$ the market price of the share at the end of the period one.

Step-two

Multiply both sides of equation (1) by the number of shares outstanding (n) to obtain the total value of the firm if no new financing exists.

$$np_c = \frac{n(D_1 + P_1)}{1 + K_e}$$

Where,

n = no. of outstanding shares at zero period.

Step-three

If the firm issues (sells) number of new shares (m) to finance the new investment needs of the fund at a price of P_1 , the value of the firm at time zero will be:

$$np_c = \frac{n(D_1 + P_1) + (nP_1 - mP_1)}{1 + K_e} \dots\dots\dots(2)$$

$$np_c = \frac{nD_1 + P_1 + nP_1 - mP_1}{1 + K_e} \dots\dots\dots(3)$$

Where,

n = no. of shares at the beginning (no. of outstanding shares at zero period.)

m = no. of equity shares issued at the end of the period.

Step-four

The investment proposals of a firm, in a given period of time can be financed, either by retained earning or the issuance of new shares or both. Thus the amount of new issued will be:

$$mp_1 = I - (E - nD_1)$$

$$\text{Or, } mp_1 = I - E + nD_1 \dots\dots\dots (4)$$

Where,

I = Investment needs

E = Earning available.

Step-five

By substituting the value of mp_1 from equation (4) to equation (3), we get,

$$np_o = \frac{nD_1 + (n+m)p_1 - I + E - nD_1}{1 + K_e}$$

$$np_o = \frac{p_1(n+m) - I + E}{1 + K_e} \dots\dots\dots(5)$$

Step-six

Conclusions: Since dividend does not appear directly in expression and E, I, $(n+m) p_1$ and k_e are assumed to be independent of dividend.

In other words, MM concludes that dividend policy is irrelevant and dividend policy has no effect in the value of the firm. A firm that pays dividends will have to raise funds externally to finance its investment plans. MM hold that when the firm pays dividends, external financing offsets its advantage.

It does not seem so relevant to apply MM approach in Nepalese Context because when we apply this approach, the assumptions supposed by MM are significantly deviated. In Nepal, we are unable to find the rational investors as well as perfect capital market, which are considered by MM. It does not seem so sound to neglect the flotation cost, transaction cost and tax effect on capital gain as neglected by MM. Arbitrage arguments as explained by MM applies only when there are very sensitive investors and which are lacking in Nepal. A conscious investor always finds different between dividend and retained earning, and generally, Nepalese investors also prefer dividends more than retained earnings, when dividend is distributed. Thus, MM proposition is not

relevant in the case of Nepal (Miller and Modigliani; 1961: 411-433, extracted from, "Panday; 1989:287").

2.2.3 Gordon's Study

Myron Gordon(1962) conducted a study on the stock valuation using the dividend capitalization approach. Gordon concludes that dividend policy does affect the value of shares even when the return on investment and required rate of return are equal. He explains that investors are not indifferent between current dividend and retention of earnings with the prospect of future dividends, capital gain and both. The conclusion of this study is that investors have a strong preference for present dividends to future capital gains under the condition of uncertainty. It is assumed that current dividend is less risky than the expected capital gain. His argument stresses that an increase in dividend payout ratio leads to increase in the stock price for the reason that investors consider the dividend yield (D_1/P_0) is less risky than the expected capital gain.

Gordon's model is also described as "a bird in hand argument". It supports the arguments which are popularly known as a bird in hand is worth two in the bush. What is available at present is preferable than what may be available in the future. That is to say current dividends are considered certain and risk less. So it is preferred by rational investors as compared to deferred dividend in future. The future is uncertain. The investors would naturally like to avoid uncertainty. So the current dividends are given more weight than expected future dividend by the investors. So the value per share increases if dividend payout ratio is increasing. This means there exist positive relationship between the amount of dividend and stock prices.

Basic assumptions of this model are as follows:

- i. The firm uses equity capital only.
- ii. Internal rate of return (r) and cost of capital (k_e) are constant.
- iii. The firm and its stream of earnings are perpetual.
- iv. There are no taxes on corporate income.

- v. The retention ratio (b) once decided upon is constant. Thus the growth rate, ($g = b_r$) is constant forever.
- vi. K_e must be greater than $g (=b_r)$ to get meaningful value.
- vii. The source of financing for new investment is only retained earning. No external financing is available.

Gordon's model is also known as GROWTH MODEL. The formula for finding out the market value per share, proposed by Gordon is given below.

$$P = \frac{E(1-b)}{k_e - b_r} = \frac{E(1-b)}{k_e - g}$$

Where,

P= Price of share / market value per share

E= Earning per share

b= Retention ratio / percentage of retained earning

1-b= Dividend payout ratio (i.e., percentage of earning distributed As dividend)

k_e = Capitalization rate / cost of capital

b_r = g or growth rate in r , (i.e., rate of return on investment of an All equity firm)

1st case: Growth Firms ($r > k$)

In the case of growth firm, the value of a share will increase as the retention ratio (b) increases and the value of a share will decrease as the retention ratio (b) decreases. I.e. high dividend corresponding to earnings leads to decrease in share prices and low dividend corresponding to earning leads to increase in share prices. So, dividends and stock prices are negatively correlated in growth firm i.e., $r > k$ firm.

2nd Case: Normal Firms: ($r=k$)

Dividend payout ratio does not affect the value of share in normal firm. In other words, share value remains constant regardless of changes in dividend

policies. It means dividend and stock price are free from each other in normal firm i.e., $r = k$ firm.

3rd Case: Decline Firms: ($r < k$)

In case of declining firms, share price tends to enhance with increase in payout ratio, $1-b$, or decrease in retention ratio, b . So, dividends and stock prices are positively correlated with each other in decline firm i.e., $r < k$ firm (Gordon. M.J; 1962: 264-272, extracted from, "Panday; 1989:287")

2.2.4 Friend and Puckett's Study

Irwin Friend and Marshall Puckett (1964) conducted a study on the relationship between dividends and stock prices. They used the regression analysis on the data of 110 firms from five industry samples, viz., chemicals ($n=20$), electronics ($n=20$), electric utilities ($n=25$), foods ($n=25$), and steels ($n=20$), in each of two years, 1956 and 1958. The industries were selected to permit a distinction to be made between the results for growth and non-growth industries and to provide a basis for comparison with results by other authors for earlier years. Both cyclical and non-cyclical industries were covered. The periods covered include a boom year for the economy when stock prices leveled off after a substantial rise (1956) and a somewhat depressed year for the economy when stock prices, however, rose strongly (1958).

They used two-regression model of price function and dividend supply function. In price function, dividends, retained earnings & price earnings ratio are independent variables, whereas, earnings, last year's dividends and price earning ratio are independent variables in dividend supply function. Symbolically, their price function and dividend supply function can be written as:

$$\text{Price function; } P_t = a + b D_t + c R_t + d (E/P)_{t-1}$$

Where,

P_t = Per share price at time t

D_t = Dividends at time t

R_t = Retained earnings at time t

$(E/P)_{t-1}$ = Lagged earnings price ratio

And, Dividend supply function;

$$D_t = e + f E_t + g D_{t-1} + h (E/P)_{t-1}$$

Where,

E_t = Earnings per share at time t

D_{t-1} = Last year dividend

The followings were the basic assumptions of their study:

1. Dividends do react to year-to-year fluctuations in earnings.
2. Price does not contain speculative components.
3. Earnings fluctuations may not sum zero over the sample.

The regression $P_t = a + b D_t + c R_t$ presents the usual simple linear relationships between average prices and dividends and retained earnings to show with the data. They found the customary strong dividend and relatively weak retained earnings effect in three of five industries i.e., chemicals, foods, and steels.

By adding lagged earnings price ratio to the above equation, they got the following results.

$$P_t = a + b D_t + c R_t + d (E/P)_{t-1}$$

They tested this equation and found the following results.

Dividends have a predominant influence on stock prices in the same three out of five industries but the differences between the dividends and retained earnings coefficients were not quite so marked as in the first set of regressions. The dividends and retained earnings coefficients were closer to each other for all industries in both years except for steels in 1956, and the correlations are higher, again except for steels.

They also calculated the dividend supply equation, i.e., $D_t = e + f E_t + g D_{t-1} + h (E/P)_{t-1}$ and derived price equation for four industry groups in 1958. The derived price equation show no significant changes from those obtained from the single equation approach as explained above, reflecting the fact that stock price, or more accurately the price earnings

ratio, does not seem to have a significant effect on dividend payout. On the other hand, they noted that, in three of the four cases tested, the retained earnings effect is increased relatively. Moreover, their result suggested that price effects on dividend supply are probably not a serious source of bias in the customary derivation of dividend and retained earnings effects on stock prices, though such a bias might be masked if the distributing effects of short run income movements are sufficiently great.

Further, they used lagged price as a variable instead of lagged earnings price ratio. They found that retained earnings received greater relative weight than dividends in the majority of the cases. The only exceptions were steels and foods in 1958. Chemicals, electronics, and utilities were considered as growth industries and the retained earnings effect was larger than the dividend effect for both years covered. For the other two industries (steels and foods) there no longer seems to be any significant systematic differences between the retained earnings and dividend coefficients.

Similarly, they tested the regression of $P_t = a + b D_t + c R_t$ by using normalized earnings again. They obtained normalized retained earnings by subtracting dividends from normalized earnings. That normalization procedure was based on the period 1950-61. Again, they added prior year's normalized earnings price variable and they compared the result. Comparing the result, they found that there was significant role of normalized earnings and retained earnings but effects of normalized price earnings ratio were constant. After examining the later equation, they found that the difference between dividend and retained earnings coefficients disappeared. Lastly, they come to know a conclusion that management might be able to increase prices somewhat by raising dividends in foods and steel industries.

At last, Friend and Puckett found a conclusion that, it is possible that management might be able, at least in some measure, to increase stock prices in non-growth industries by raising dividends, and in growth industries by greater retention, i.e. smaller (lower) dividends.

2.2.5 Walter's Study

James E. Walter (1966) conducted a study on dividend and stock prices. He proposed a model for share valuation. According to him, the dividend policy of the firm affects the value of the shares. So, the dividends are relevant. He argues that the choice of dividend policies always affect the value of enterprise.

His study shows clearly the importance of the relationship between internal rate of return (R) and its cost of capital (K) in determining the dividend policy.

The assumptions of the Walter's model are as follows:

- Firm finances all investment through retained earning. The external funds (i.e. debt, new equity) are not used for new investment.
- All earning on the firm's investment (R) and the cost of capital (k) are constant.
- All earnings are either distributed as dividend or reinvested internally.
- The values of EPS and DPS are assumed to remain constant forever in determining a given value.
- The firm has a perpetual or infinite life.

Based on these above assumptions, Walter has given following formula of valuation of equity share.

$$P = \frac{DPS}{K_e} + \frac{r/k_e(EPS-DPS)}{K_e}$$

Where,

P = market value of an equity share
(Market price per share)

DPS = Dividend per Share

EPS = Earning Per Share

r = The rate of return on the firm's investment.

k_e = cost of capital / capitalization rate

According to Walter's model, the optimum dividend policy depends on the relationship between the firm's internal rate of return (r) and its cost of capital (k). Walter referred different dividend policy for different types of the firm which can be summarized as follows.

Growth Firm ($r > k$)

Growth firms are those firms, which expand rapidly. Because of ample investment opportunities yielding return (r) is higher than the opportunity cost of capital (k). So, firms having $r > k$ are referred as growth firms which are able to reinvest earnings at a rate which is higher than the rate expected by shareholders. They will maximize the value per share if they follow a policy of retaining all earnings for internal investment. Thus, the correlation between dividend and stock price is negative, and the optimum payout ratio for a growth firm is zero. The market value per share (P), increases, as payout ratio declines when $r > k$.

Normal Firm ($r = k$)

If the internal rate of return is equal to cost of capital, the dividend payout does not affect the value of share, i.e. dividends are indifferent from stock prices. In other words, there is no role of dividends on stock prices. Such a firm can be called as a normal firm. Whether the earnings are retained or distributed as dividend, it is a matter of indifference for a normal firm. The market price of share will remain constant for different dividend payout ratio from zero to 100. Thus, there is no unique optimum payout ratio for a normal firm. One dividend policy is good as other and the market value per share is not affected by the payout ratio when $r = k$.

Declining Firm ($r < k$)

If the internal rate of return (R) is less than cost of capital (k), it indicates that the shareholders can earn a higher return by investing elsewhere. In such a case for maximizing the value of shares, dividend also should be maximized. By distributing the entire earning as dividend, the value of share will be at optimum value. In other words, the market value per share of a declining firm

with $r < k$ will be maximum when it does not retain earnings at all. The relation between dividends and stock price is positive. The optimum payout ratio for a declining firm is 100 percent and the market value per share increases as payout ratio increases when $r < k$.

Criticism of Walter's Model

(i) No external financing

This model is based on assumption that the investment opportunities of the firm are financed by retained earnings finance the investment opportunities of the firm only no external financing i.e., debt or equity is used for the purpose. When such a situation exist either the firm's investment or its dividend policy or both will be sub-optimum.

(ii) Constant rate of return (R) and opportunity cost of capital (K)

This model assumes that rate of return (R) and opportunity cost of capital or discount rate (k) is constant. In fact, rate of return (R) changes with increase and decrease of investment. i.e., R decreases as more investment occurs and cost of capital (k) changes directly with the risk borne by the firms. (Walter; 1966: 29-41, extracted from, "Panday; 1989:280").

2.2.6 Van Horne And Donald's Study

Van Horne and Mc-Donald (1971) conducted a study on dividend policy and new equity financing. The purpose of this study was to investigate the combined effect of dividend policy and new equity financing decision on the market value of the firm's common stocks.

Empirical tests are performed with year end 1968 cross sections for two industries, using a well-known valuation model. For there investigation, they employed two samples of firms viz. the 86 electric utilities in the continental U.S. which are included on the COMPUSTAT utility data tape; and 39 companies in the electronics and electric component industries as listed on the COMPUSTAT industrial data tape in 1968.

They performed empirical study by testing two regressions for the electric utilities and one regression model for electronics and electronic components industry.

They concluded that for electric utility firms in 1968, share value was not adversely affected by new equity financing in the presence of cash dividends, except for those firms in the highest new issue group and it made new equity a more costly form of financing than the retention of earnings.

They also indicated that the "Cost" disadvantages of new equity issues relative to retained earnings widens as relatively large amounts of new equity are raised, so that the payment of dividends through excessive equity financing reduces share prices. For firms in the electronics-electronic component industry, a significant relationship between new equity financing and value was not demonstrated.

2.2.7 Chawla and Srinivasan's Study

Deepak Chawla and G.Srinivasan(1987) conducted a study on the impact of dividend and retention on share price. They selected 18 chemicals and 13 sugar companies and estimated cross-sectional relationship for the years 1969 and 1973. They collected the required data from the official directory of Bombay stock exchange. They used two stages least square technique for estimation. They also used lagged, earnings price ratio instead of lagged price earnings ratio, i.e. $P/E_{(t-1)}$.

The followings were the prime objectives of their study.

- (i) To test the hypothesis of dividend and retained earnings.
- (ii) To estimate a model to explain share price, dividend and retained earnings relationship.
- (iii) To examine the structural changes in estimated relations over time.

In order to achieve (attain) these objectives, they used simultaneous equation model as developed by Friend and Puckett (1964). The following was the model in its unspecified form.

1. Price function

$$P_t = f [D_t, R_t, P/E_{(t-1)}]$$

2. Dividend supply function

$$D_t = f [E_t, D_{(t-1)}, P/E_{(t-1)}]$$

3. Identity,

$$E_t = D_t + R_t$$

Where,

P= market price per share.

D= Dividend per share.

R= Retained earning per share.

E= Earning per share (D+R)

P/E= Deviation from the sample,

(Average of price earning ratio)

t= subscript of time.

It was found, from the result of their two stages least square estimation, that the estimated coefficients had the correct sign and the coefficients of determination of all the equations were very high in case of chemical industry. It implies that the stock price and dividend supply variation can be explained by their independent variables. But in case of sugar industry, they found that the sign for retained earnings is negative in both years and left for further analysis of sugar industry.

It was observed that the coefficient of dividend was very high as compared to retained earnings for chemical industry. They also found that coefficient of dividend was significant at one percent level in both years whereas coefficient

of retained earnings was significant at ten percent level in 1969 and one percent level in 1973.

Finally, they concluded that dividend hypothesis holds well in the chemical industry. Both dividend and retained earnings significantly explain the variation in share price in chemical industry. They also stressed that the impact of dividend is more pronounced than that of the retained earnings but the market has started shifting towards more weight for retained earnings.

2.2.8 Michaely, Thaler & Womack's Study

R. Michaely, Richard H. Thaler & Kent L. Womack (1995) conducted a study on price reactions to dividend initiations and omissions. They investigated the immediate and long-term effects of dividend initiation & omission announcements. They found that the short – run price impact of dividend omissions was negative and that of initiations was positive. Initiation reactions were about one-half the magnitude of the market reaction to omission announcements. The change in yield, however, was about seven times larger for the omission announcements. They saw that the market reaction to a dividend omission announcement was no greater than to an initiation for a given change yield.

2.3 Review of Related studies

2.3.1 Review of Journals and Articles in Nepalese Perspective

Dr. M. K. Shrestha (1981) in his article “*Public Enterprises: Have They Dividend Paying Ability?*” highlighted (focused) the following issues in the article.

Government wants two things from the public enterprises:

They should be in a position to pay minimum dividend & Public enterprises and should be self-supporting in financial matters in future years to come. But these both objectives are not achieved by public enterprises.

1. One reason for this inefficiency is caused by excessive governmental interference over daily affairs even though there is provision of government interference only for policy matters. On the other hand, high-ranking officials of Nepal Government appointed as directors of board do nothing but simply show their bureaucratic personalities, Bureaucracy has been the enemy of efficiency and thus led corporation to face losses. Losing corporations are, therefore, not in a position of pay dividends to government.
2. Another reason of this is the lack of self-criticism and self-consciousness (Shrestha; 1981:13).

Dr. M. K. Shrestha (1992) in his article “*Shareholders’ Democracy and Annual General Meeting Feedback*” has dealt with the policies and financial performance of some financial companies and has made the following outcomes:

- i. The cost-push inflation at exorbitant rate has made the shareholders to expect higher return from their investment.
- ii. Multiple decrease in the purchasing power of the Nepalese currency to the extent that higher return by way of dividend is just a natural economic consequence of it.
- iii. Erosion in the purchasing power of the income has made it clear that dividend payment must be directed to enhance shareholders' purchasing power by raising dividend payout ratio on the basis of both earnings and cost theory.
- iv. Indo-Nepal trade and transit deadlock has become a sort of economic warfare putting rise in the cost of living index to a considerable extent. This is one of the reasons, which made shareholders to expect higher demand for satisfactory dividend.
- v. The waiting of five years with peanut dividend in previous year is equally a strong enforceable reason of the bank's shareholders to expect handsome dividend already assured and committed in various reports of the earlier annual general meeting.

- vi. One way to encourage risk-taking ability and preference is to have proper risk- return trade off by bank's management board in a way that higher return must be the investment rule for higher risk-takers that comprise bank's shareholders (Shrestha;1992:34-35).

2.3.2 Review of Thesis

Nabaraj Adhikari (1996) “*Corporate Dividend Practices in Nepa.*” The specific objectives of his study are:

- (a) To analyze the properties of portfolios formed on dividends.
- (b) To examine the relationship between dividends and stock prices.
- (c) To survey the opinions of financial executives on corporate dividend practices.

The methodology used in the study includes financial tools such as ratio analysis and statistical tools such as correlation co-efficient and probable error. Secondary data are used for the analysis.

Conclusion of his study is that there are differences in financial position of high dividend paying and low dividend paying companies. Other things remaining the same, financial position of high dividend paying companies is comparatively better than that of low dividend paying companies. Another interesting conclusion of his study is that market price of shares affected by dividends. Lastly, financial executives of Nepal reject dividend as a residual decision in Nepalese companies (Adhikari; 1996).

Rishi Raj Gautam (1996) “*Dividend Policy in Commercial Banks, A Comparative Study of NGBL, NIBL and NABIL*”

Main objectives of this study are:

- To identify what type of dividend policy is being followed and find out whether the policy followed is appropriate or not.

- To examine the impact of dividend on share prices.
- To identify the relationship between DPS and other financial indicators.
- To know if there is any uniformity among DPS, EPS and DPR of the three sample commercial banks.

The methodology used in the study includes financial tools such as ratio analysis and statistical tools such as correlation coefficient and probable error. Secondary data are used for the analysis.

The major Findings of his study are:

- Average earnings per share and dividend per share of all concerned banks are satisfactory.
- Analysis indicates that there is the largest fluctuations in EPS and DPS and have relatively more consistency dividend per share in all the three banks.
- No commercial banks seen to be guided by clearly defined dividend strategy in spite of the good earnings and potentials.
- Shares of the financial institution are actively traded and market prices are increasing.
- Commercial banks represent a robust body of profit earnings organization in comparison to the other sectors such as manufacturing, trading etc.
- One of the most striking findings of this study is that no commercial bank sample for this study has clearly dividend strategy. On the other hand, there is significant relationship perceives between earnings and dividend of expansion program.

Prerana Laxmi Rajbhandari (2001) *“Dividend Policy: A comparative Study between Banks and Insurance Cos.”*

The main objective of her study is to find out the appropriate dividend policies and practices in Nepal.

The specific objectives of her study are:

- a) To examine the relationship between dividend and market price of the stock.
- b) To identify the appropriate dividend policy followed by the banks and insurance companies.
- c) To analyze the relation between dividend policy decision of banks and insurance companies.

The methodology used in the study includes financial tools such as ratio analysis and statistical tools such as correlation co-efficient and probable error. Secondary data are used for the analysis.

Conclusion other study is that no consistency in dividend payment is found in all the sample institutions i.e. NGBL, NIRL, NABIL, NIC. and EIC which seems to be paying average DPS Rs20 every year. This shows that none of the six sample institutions have a clearly defined and appropriate dividend policy. The institutions don't seem to follow the optimal dividend policy of paying regular dividend as per the share holder's expectation and interest. This would create uncertainty among the shareholders. The major findings has also led to conclude the controversy existed in declaring dividend by the companies in the sense that the major factors like the firm have been neglected, ignored and disregarded which must have been considered the most.

Subhash Kunwar(2001) *“Dividend Policy: A comparative Study between Nepal Insurance Co. Ltd. and National and General Insurance Co. Ltd.”*

The main objectives of his study are:

- a. To examine the influence of financial indicators on share price.
- b. To show the relationship between dividend per share and other financial indicators.
- c. To check the consistencies amongst DPS, EPS, D/P ratio etc. of the sample insurance company.
- d. To identify the dividend policy undertaken by each company and the appropriateness of the policy undertaken.

- e. To provide useful suggestions to formulate optimal dividend policy and maximize stock price on the basis of findings.

The methodology used in the study includes financial tools such as ratio analysis and statistical tools such as correlation co-efficient and probable error. Secondary data are used for the analysis.

Conclusion of his study there are many factors that influence the dividend and the market value of share such as earnings, liquidity position, efficiency, and leverage. These factors indicate the financial position of the company. If the company has good performance in terms of these factors it will be able to provide returns in the form of dividends to its Shareholders.

Yagya Bahadur Katawal (2001) "*A Comparative Study Of Dividend Policy in Commercial Bank*" The main objectives of this study are:

- To study the current practices of dividend policy in commercial banks.
- To find out the impact of dividend on share prices.
- To analyze the relationship of financial indicators.
- To examine if there is any uniformity among DPS, EPS and DPR on the six sample banks.

The methodology used in the study includes financial tools such as ratio analysis and statistical tools such as correlation co-efficient and probable error. Secondary data are used for the analysis.

The major findings of this study are:

- Average EPS and DPS for the period covered by the study of all concerned banks are satisfactory.
- Analysis of coefficient of variance indicates that there is large fluctuation in EPS and DPS and other are relatively more consistent.
- The analysis of DPR shows that none of the sample banks have consistent dividend policy.
- The market value of shares in market is fluctuating in all sample banks.

- The most important decision is that no specific dividend payment strategy is followed by these banks. Payment of cash dividend and stock dividend are made without wise managerial decision due to unstable and adequate dividend and unequal payout ratio.

Pravin Kumar Ghimere (2002) “*Dividend policy of listed companies with ref. to banks, finance and insurance companies.*”

The main objectives of his study are:

- To identify the dividend policy of different sample companies.
- To identify the regularity of divided distribution of different listed companies.
- To identify the relationship between dividend policy and other financial indicators.
- To find out whether dividend policy affect the value of the firm or not.
- To analyze the relationship between DPS and MPS.
- To provide suggestion for the improvement of sample companies dividend policy on the basis of findings.

The methodology used in the study includes financial tools such as ratio analysis and statistical tools such as correlation co-efficient and probable error. Secondary data are used for the analysis.

The major findings:

- The average dividend per share of the banks is satisfactory compared to finance and insurance companies.
- The average earning per share of the bank is also more satisfactory than finance and insurance companies.
- DPS of the finance companies are more fluctuating in comparison to banks among them HBL has more fluctuation and NGBL being consistent.

- Dividend yield of the finance and insurance are higher than banks and more consistent too.
- Banks are following aggressive dividend policy due to higher DPR whereas finance and insurance companies implemented moderate dividend policy.

Raju Karki (2006) conducted research on, “A Study on Dividend Policy in Finance Companies.” The main objectives of the research are;

- To analyze the dividend policy followed by Finance companies.
- To compare the dividend paid by Annapurna Finance Company Ltd. and Butwal Finance Ltd.
- To examine the relationship between DPS with EPS, MPS and BPS.
- To predict DPS in future years.

The major findings of Karki are as follows;

- The shareholders of AFCL enjoyed higher DPS than those of BFL.
- AFCL made more EPS than BFL. However, DPR of BFL is higher than DPR of AFCL, which indicates that BFL has concentrated on attracting new shareholders by distributing more portion of its earning while AFCL focused on retaining earning for internal financing.
- There is high positive relationship between DPS and EPS of AFCL and the relationship is statistically significant. However, the relationship between DPS and EPS of BFL is positive but the relationship is insignificant.
- The correlations coefficient indicates that MPS increases with the increase in DPS of each bank and the relationship is positively significant.
- The regression analysis indicates that the MPS of both banks is highly dependent on the DPS and EPS of corresponding banks.

- The trend analysis depicts that the DPS of AFCL in the fiscal year 2005/06 and 2006/07 will be Rs.12.76 and Rs.14.85 respectively, whereas the DPS of BFL will be Rs.9.82 and Rs.10.15 in the fiscal year 2005/06 and 2006/07 respectively.

Ajay Raj Khatiwada (2008) conducted research on, “A comparative study of Dividend policy in Nepal Investment Bank Ltd. and Standard Chartered Bank Ltd.” The main objectives of the research are;

- To identify the dividend policy in SCBNL and NIBL.
- To examine the relationship between earning and dividend distribution.
- To evaluate the impact of dividend on share price.
- To examine the relationship of DPS with other financial indicators.

Aryal presented the following major findings in his study.

- The shareholders of SCBNL received comparatively very high DPS than the shareholders of NIBL. On average, SCBNL paid Rs.110 DPS, whereas NIBL paid Rs.14.50 DPS.
- SCBNL remained more successful than NIBL in generating earning per share. On average, SCBNL earned Rs.155.84 per share, while NIBL earned only Rs.50.54.
- The DPR of SCBNL is also very high compared to that of NIBL. The average DPR of SCBNL is 70.59% and that of NIBL is 28.69%.
- DPS has high influence on the price rise/fall of share. Both MPS and BPS are highly dependent on the DPS of corresponding banks.
- The prime objective to invest in bank is to earn dividend. About 78% of the respondents stated that dividend is the most alluring factor in share investment.
- There exists high correlation between DPS and EPS, DPS and MPS and DPS and BPS of both banks.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Introduction

A brief introduction of this study has been already presented in the first chapter. Besides the review of the ideas, theories and research findings have also been presented in second chapter. Now it is important to have a look into research methodology that helps to make this analysis meaningful.

This chapter highlights the method of research adopted in this study. Research design, sample selection, data collection procedure, period covered, data processing procedure and tools used for analysis are included under this chapter.

The analytical as well as descriptive research designs have therefore been included in the present study. In this study, research methodology has been paid due attention to achieve the objectives of the study.

3.2 Research Design

The main objective of this research work is to evaluate the dividend policy of Bank of Kathmandu Limited (BOK) and Everest Bank Limited (EBL). To complete this study, following design and format has been adopted.

First of all, information and data are collected. The important information and data are selected. Then data are arranged in useful manner. After that, data are analyzed by using appropriate financial and descriptive and analytical tools. In analysis part, interpretation and comments are also made wherever necessary.

3.3 Sources of Data

The study is based on secondary data. The secondary data are collected from their respective annual reports especially from profit and loss accounts, balance sheet and other publications made by the banks. Likewise, some other related

information is gathered from related banks and related agencies like Nepal Rastra Bank, Nepal Stock Exchange Limited.

3.4 Population and Sample

At present, there are 25 commercial banks operating in Nepal. Due to time and resource factors, it is not possible to study all of them regarding the study topic. Therefore, sampling will be done selecting from population.

The samples to be selected are as follows:

- (i) Bank of Kathmandu Ltd.
- (ii) Everest Bank Ltd.

3.5 Period of the study

The study is based on five years financial data of sample banks (i.e., Bank of Kathmandu Limited & Everest Bank Limited) from fiscal year 2002/03 to 2006/07.

3.6 Research Tools

To achieve the objectives of the research, the following financial and statistical tools will be used.

3.6.1 Financial Tools

Earning Per Share (EPS)

Earning per share refers the rupee amount earned per share of common stock outstanding. It measures the return of each equity shareholders. It is also identified to measure the profitableness of the shareholders investment. The earning per share simply shows the profitability of the banks on a per share basis. The higher earning indicates the better achievements of the profitability of the banks by mobilizing their funds and vice versa. In other words, higher earning per share denotes the strength and lower earning per share indicates the weakness of the banks.

EPS is computed to know the earnings capacity and to make comparison between concerned banks. This ratio can be computed by dividing the earning

available to common shareholders by the total number of common stock outstanding of banks. Thus,

$$\text{EPS} = \frac{\text{Earning available to common stock holders}}{\text{Number of common stock outstanding}}$$

Dividend Per Share (DPS)

Dividend per share indicates the rupee earnings actually distributed to common stockholders per share held by them. It measures the dividend distribution to each equity shareholders.

The DPS simply shows the portion of earning distribution to the shareholders on per share basis. Generally, the higher DPS creates positive attitude of the shareholders toward the bank, which consequently helps to increase the market value of the shares. And it also works as the indicator of better performance of the bank management.

It is defined as the result received by dividing the total dividend distributed to equity shareholders by the total number of equity shares outstanding. Thus,

$$\text{DPS} = \frac{\text{Total amount of dividend paid to ordinary shareholders}}{\text{Number of ordinary shares outstanding}}$$

Bonus Share Dividend (BSD)

Bonus share dividend is the rupee bonus share distributed in case of cash dividend. It is the distribution of share for share as a dividend. It can be calculated as:

Dividend Payout Ratio (DPR)

It is the portion of the earning used for the payment of dividend. The dividend payout ratio is the earnings paid to the equity holders from the earnings of a firm in a particular year. This ratio shows what percentage of the profit is

distributed as dividend and what percentage is retained as reserve and surplus for the growth of the banks. In other words, the amount of dividend that a bank pays depends upon the earning capacity of the bank. Higher earning enhances the ability to pay more dividends and vice versa.

There is a reciprocal relationship between dividends and retained earnings, the higher the dividend payout ratio, the lower will be the retained earnings and hence the capacity of internal financing of the firm is checked.

It is calculated to indicate the percentage of the profit that is distributed as dividend. This ratio is calculated by dividing dividend per share by the earning per share. Thus,

$$\text{DPR} = \frac{\text{Dividend per share}}{\text{Earning per share}}$$

$$\begin{aligned}\text{And, retention ratio} &= (1-\text{Dividend payout ratio}) \\ &= (1-\text{DPR})\end{aligned}$$

Price-Earning Ratio (P/E Ratio)

Price-earning ratio is also called the earnings multiplier. Price-earning ratio is simply the ratio between market price per share and earning per share. In other words, this represents the amount which investors are willing to pay for each rupee of the firm's earnings.

The P/E ratio measures investor's expectation and market appraisal of the performance of firm. This is important to compare the market share prices of different stocks given their earning per share. The higher P/E ratio implies the high market share price of a stock given the earning per share and the greater confidence of investor in the firm's future. This ratio is computed by dividing earning per share to market price per share. Thus,

$$\text{P/E Ratio} = \frac{\text{Market price per share}}{\text{Earning per share}}$$

Earning Yield and Dividend Yield (EY and DY Ratio)

The earning yield and dividend yield both are expressed in terms of the market value (price) per share. Earning yield and dividend yield are two important profitability ratios from the point of view of the ordinary shareholders.

Earning yield (EY)

Earning per share as the percentage of market price per share in the stock market is called the earning yield. In other words, it is a financial ratio relating to earning per share to the market share price at a particular time. It measures the earning in relation to market value of share. It gives some idea of how much an investor might get for his money.

The share with higher earnings yield is worth buying. Earning yield is informative to compare the market share prices of stocks in the secondary market. It is calculated as:

$$\text{EY Ratio} = \frac{\text{Earning per share}}{\text{Market price per share}}$$

Dividend Yield (DY)

Dividend yield is a percentage of dividends per share on market price per share. It shows that how much is the dividend per share on market price per share. It measures the dividend in relation to market value of share. So, dividend yield is the dividend received by the investors as a percentage of market prices per share in the stock market.

This ratio highly influences the market price per share because a small change in dividend per share can bring effective change in the market value of the share. The share with higher dividend yields is worth buying. Dividend has

important guidance to commit funds for buying of shares in the secondary market. This ratio is calculated by dividing dividend per share by market price of the stock. Thus,

$$\text{DY Ratio} = \frac{\text{Dividend per share}}{\text{Market price per share}}$$

Market Value (Price) Per Share to Book Value Per Share (MPS to BVPS) Ratio

This ratio measures that the market situation per share in the competitive open market with respect to book value per share of joint venture banks. This ratio indicates the price that the market is paying for the share that is reported from the net worth of the banks.

This is important to compare the market share prices of different stocks on the basis of the book value per share. It shows the market share price of a stock as a percentage of book value per share and the effect of later on the former. The higher ratios represent to conclude that the better performance of joint venture banks in terms of market price per share to book value per share. This ratio can be derived by dividing market price per share by book value per share. Thus,

$$\text{MPS to BVPS Ratio} = \frac{\text{Market price per share}}{\text{Book value per share}}$$

3.6.2 Statistical Tools

- Mean or Average, Standard Deviation & Coefficient of Variation.
- Coefficient of Correlation & Coefficient of Determination.
- Regression Analysis.
 - (i) Regression constant – (a)
 - (ii) Regression coefficient – (b)

Arithmetic Mean or Average (\bar{X})

An average is a single value that represents a group of values. It depicts the characteristic of the whole group. It is a representative of the entire mass of homogeneous data, its value lies somewhere in between the two extremes, i.e. the largest and the smallest items. It is obtained by dividing the sum of the quantities by the number of items. Thus,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N}$$

Where,

$\sum X$ = sum of the sizes of the items

N = number of items

Standard Deviation: (S.D.)

The concept of standard deviation was first introduced by Karl Pearson in 1983. It is the most usual measure of dispersion and it represents the square root of the variance of a group of numbers, i.e., the square root of the sum of the squared differences between a group of numbers and their arithmetic mean. In other words, standard deviation is the positive square root of the arithmetic average of the squares of all the deviations measured from the arithmetic average of the series. It is independent of the position of the origin. Generally, it is denoted by small Greek letter σ (read as sigma) and is obtained as follows.

$$\text{Standard Deviation } (\dagger) = \sqrt{\frac{\sum (X - \bar{X})^2}{N}}$$

Where,

N = Number of items in the series.

\bar{X} = mean

X = Variable

The standard deviation measures the absolute dispersion or variability of a distribution; the greater the amount of dispersion or variability the greater the standard derivation, for the greater will be the magnitude of the deviations of

the values from their mean. A small standard deviation means a high degree of uniformity of the observation as well as homogeneity of a series.

Coefficient of Variation (C.V.)

Karl Pearson developed this measurement to measure the relative dispersion. It is used in such problems where we want to compare the variability of two or more series. The series (or group) for which the coefficient of variation is greater is said to be more variable or conversely less consistent, less uniform, less stable or less homogeneous. On the contrary, that series (or group) for which the coefficient of variation is less is said to be less variable or more consistent, more uniform, more stable or more homogeneous. It is denoted by C.V. and is obtained by dividing the arithmetic mean to standard deviation. Thus,

$$\begin{aligned}\text{Coefficient of Variation (C.V.)} &= \frac{\text{SD} \times 100}{\text{Mean}} \\ &= \frac{\sigma \times 100}{\bar{X}}\end{aligned}$$

Where,

σ = Standard Deviation

\bar{X} = Mean

Coefficient of Correlation

According to Richard I. Levin, "correlation analysis is the statistical tools that we can use to describe the degree to which one variable is linearly related to another" (Levin and David; 1994:613).

The correlation analysis refers to the techniques used in measuring the closeness of the relationship between the variables. It helps us in determining the degree of relationship between two or more variables. It doesn't tell us anything about cause and effect relationship. It describes not only the

magnitude of correlation but also its direction. The coefficient of correlation is a number, which indicates to what extent two things (variables) are related to what extent variations in one go with the variations in the other.

The value of coefficient of correlation as obtained shall always lie between ± 1 , a value of -1 indicating a perfect negative relationship between the variables, of $+1$ a perfect positive relationship, and of no relationship when correlation coefficient is zero. The zero correlation coefficient means the variables are uncorrected.

Similarly, a high correlation coefficient reveals that two variables move together but doesn't indicate cause and effect. In other words, the closer r is to $+1$ or -1 , the closer the relationship between the variables and closer r is to zero (0), the less close relationship. The algebraic sign of the correlation coefficient indicates only the direction of the relationship between two variables, whether direct or inverse, while the numerical value of the coefficient is concerned with the strength, or closeness of the relationship between two variables.

Thus, in this study, the degree of relationship between dividend and other relevant financial indicators such as earning per share, market price per share, current ratio, net profit & net worth is measured by the correlation coefficient, which is denoted by r or r_x or r_{yx} (of X and Y are two sets). It is defined by Karl Pearson as:

$$r = \frac{N \sum XY - \sum X \sum Y}{\sqrt{N \sum X^2 - (\sum X)^2} \sqrt{N \sum Y^2 - (\sum Y)^2}}$$

Under the correlation analysis, the following financial variables have been calculated.

Simple Correlation Coefficient.

- a) Between dividend per share and earning per share.
- b) Between market price per share and dividend per share.

- c) Between Book value per share and dividend per share.
- d) Between earning yield and dividend yield.
- e) Between market price per share and dividend payout ratio.

Multiple correlation coefficients:

- a) Between market price per share (MPS) and earning per share (EPS), dividend per share (DPS).

Coefficient of Determination

The coefficient of determination is the primary way. We can measure the extent, or strength, of the association that exists between two variables, X and Y. R^2 measures only the strength of a linear relationship between two variables. It refers to a measure of the total variance in a dependent variable that is explained by its linear relationship to an independent variable. The coefficient of determination equals R^2 and the value of R^2 lies between zero and unity, the closer to unity, the greater the explanatory power. A value of one can occur only if the unexplained variation is zero, which simply means that all the data points in the scatter diagram fall exactly on the regression line. The R^2 is always a positive number. It can't tell whether the relationship between the two variables is positive or negative. The R^2 is defined as the ratio of explained variance to the total variance. Thus,

$$\text{Coefficient of determination (R}^2\text{)} = \frac{\text{Explained Variance}}{\text{Total variance}}$$

$$\text{Or, R}^2 = \frac{1 - \text{Unexplained Variance}}{\text{Total Variance}}$$

Regression Analysis

The concept of regression was first introduced by Francis Galton. Regression refers to an analysis which is involving the fitting of an equation to a set of data points, generally by the method of least square. In other words the regression is

a statistical method for investigating relationships between the variables by the establishment of an approximate functional relationship between them. It is considered as a useful tool for determining the strength of relationship between two (Simple Regression) or more (Multiple regression) variables. It helps to predict or estimate the value of one variable when the value of other variables is known. In order to make easier in my study, regression analysis has been divided into two parts.

Simple regression

The analysis, which is used to explain the average relationship between two variables, is known as simple linear regression analysis. In this study, the following simple regression has been analyzed.

Simple Regression Analysis

1) Dividend per share on Earning per share

$$Y = a + bX$$

Where,

Y = Dividend per share

a = Regression constant

b = Regression coefficient

X = Earning Per share

This model has been constructed to examine the relationship between dividend per share (dependent variable) and earning per share (independent variable). It enables to determine whether the variable of earning per share is the influencing factor to dividend decision or not.

2) Average stock price on Dividend per share

$$Y = a + bX$$

Where,

Y = Average stock price

a = Regression constant

b = Regression coefficient

X= Dividend per share

This model examines the relationship between the average stock price and dividend per share.

3) Dividend per share on Book value per share

$$Y = a + bX$$

Where,

Y= Dividend per share

a= Regression constant

b= Regression coefficient

X= Book value per share

The relationship between book value per share and dividend per share can be explained through this model.

4) Dividend Yield on Earning Yield

$$Y = a + bX$$

Where,

Y= Dividend Yield

a= Regression constant

b= Regression coefficient

X= Earning Yield

The relationship between dividend yield and earning yield can be explained through this model.

5) Average stock price on Dividend payout ratio

$$Y = a + bX$$

Where,

Y= Average stock price (Market price per share)

a= Regression constant

b= Regression coefficient

X= Dividend payout ratio.

This model tests the dependency of market price per share on dividend payout ratio.

Multiple Regression

In multiple regression analysis, two or more independent variables are used to estimate the values of dependent variable. It is the extension of simple regression technique.

(a) Market price per share on Earning per share and Dividend per share

$$X_1 = a_1 + b_1X_2 + b_2X_3$$

Where,

X_1 = Market price per share

a_1 = Regression constant

b_1 = Regression coefficient of variable 1st

b_2 = Regression coefficient of variable 2nd

X_2 = Dividend per share

X_3 = Earning per share

It helps to predict the market price per share on earning per share and dividend per share.

(i) Regression constant (a)

The value of constant is the intercept of the model, when the independent variables are zero; it indicates the average level of dependent variable. In other word, it is better to understand that 'a' (constant) indicates the mean or average effect on dependent variable if all the variables omitted from the model.

(ii) Regression Coefficient ($b_1, b_2 \dots$)

The regression coefficient of each independent variable shows the relationship between that variable and value of dependent variable, holding constant the effect of all other independent variables in regression model. In other words, the coefficients explain how changes in independent variables affect the values of dependent variables estimate.

CHAPTER IV

DATA PRESENTATION AND ANALYSIS

This chapter consists presentation and analysis of secondary data related with different variables using both financial and statistical tools explained in the third chapter. The prime objective of this chapter is to achieve the objectives, which are set in the first chapter. In order to achieve these objectives, the gathered data are presented, compared and analyzed with the help of different tools.

4.1 Earning Per Share (EPS)

Earning per share shows the company's capability of generating profit per share. Higher EPS indicates better performance of the companies and company with net loss will result negative EPS. The EPS of both the banks, EBL & BOK is presented in the Table 4.1.

Table 4.1
Earning Per Share (EPS)

Year	EBL	BOK
2002/03	29.90	17.72
2003/04	45.60	27.50
2004/05	54.20	30.10
2005/06	62.80	43.67
2006/07	78.40	43.50
Total	270.90	162.49
Average	54.18	32.50
S.D.(†)	16.27	9.95
C.V. %	30.04	30.62

(Source: Annual report of EBL and BOK)

The table 4.1 shows that the EPS of EBL followed increasing trend during the period taken for research. The EPS of EBL ranged from Rs. 29.90 per share in the fiscal year 2002/03 to Rs. 78.40 per share in the fiscal year 2006/07. The company enjoyed higher EPS in each year compared to the EPS of previous year. The average EPS is Rs. 54.18, standard deviation is 16.27, and the coefficient of variation is 30.04%. This coefficient of

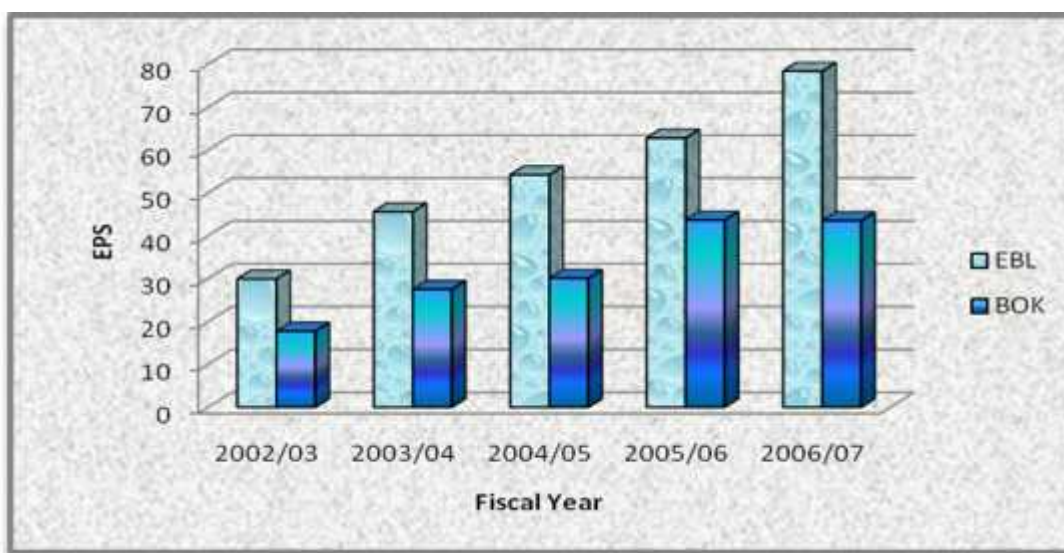
variation clears that there is 30.04% fluctuation in EPS, which means the EPS of EBL is inconsistent.

The EPS of 2002/03 and 2003/04 are lower than the average EPS of this bank. In other words, this bank is not able to maintain its average EPS for two base years, and EPS of rest three years 2004/05, 2005/06 and 2006/07 are higher than the average EPS.

Similarly, the EPS of BOK has followed the increasing trend from the base year 2002/03 except in the fiscal year 2006/07, when there is slight decrease of EPS by Rs. 0.17 compared to the EPS of fiscal year 2005/06. The EPS of BOK in the fiscal year 2002/03, 2003/04, 2004/05, 2005/06 and 2006/07 are Rs. 17.72, Rs.27.50, Rs.30.10, Rs.43.67 and Rs.43.50 respectively. Likewise, the average EPS of BOK in these five fiscal years is Rs.32.50 and the standard deviation & Coefficient of Variation are 9.95 and 30.62% respectively.

In average, EBL enjoyed higher EPS (Rs.54.18) than that of EBL (Rs.32.50). Also, there is more consistency in the EPS of EBL than that of BOK, as C.V. of EBL (30.04) is lower than the C.V. of BOK (30.62). So, it can be considered that EBL remained more successful than BOK in generating higher EPS.

Figure 4.1
Earning Per Share



4.2 Dividend per share (DPS)

Dividend per share is the amount of dividend distributed to the shareholders for the single unit of share. Higher the amount of DPS retains the shareholder for long term. However, only cash dividend distributed to the shareholders of EBL and BOK is presented in the Table 4.2.

Table 4.2

Dividend Per Share

Year	EBL	BOK
2002/03	20	5
2003/04	20	10
2004/05	0	15
2005/06	25	18
2006/07	10	20
Total	75	68
Average	15.00	13.60
S.D.(†)	8.94	5.46
C.V.	59.63	40.17

(Source: Annual report of EBL and BOK)

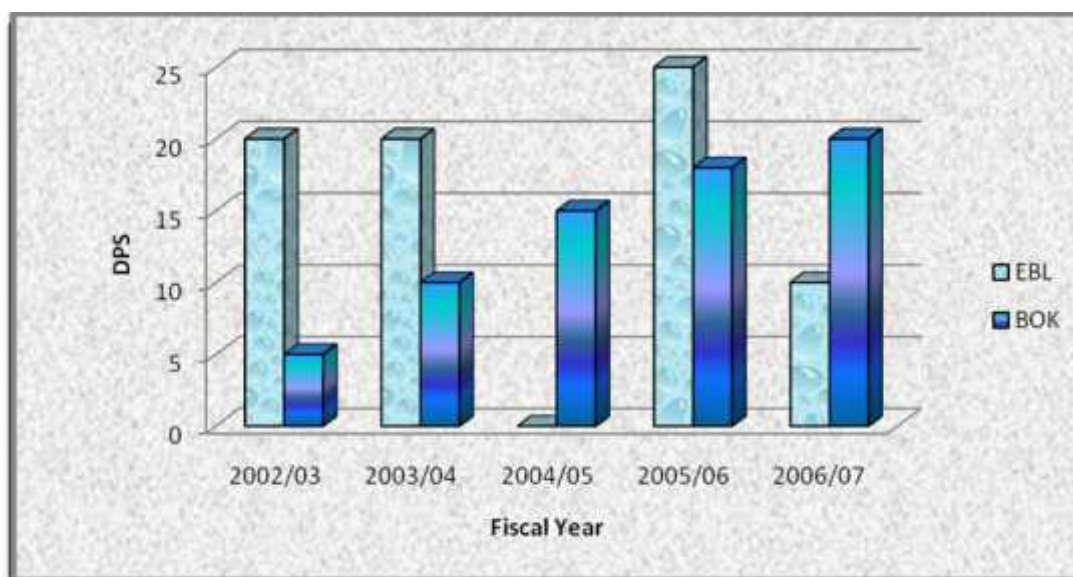
The cash dividend per share shown in the table 4.2 reflects that DPS of EBL has ranged between zero (0) to Rs.25. Similarly, EBL has not paid any cash dividend in the fiscal year 2004/05. Despite the profit, EBL has paid no

profit as dividend, which indicates that EBL has retained all the earnings for its internal growth in the fiscal year 2004/05. In the fiscal year 2002/03, 2003/04, 2005/06 and 2006/07, EBL has paid a dividend of Rs.20, Rs.20, Rs.25 and Rs.10 respectively. In average, EBL paid cash dividend of Rs.15.00 in the entire period taken for research. The standard deviation and the coefficient of variation of the bank are 8.94 and 59.63% percent respectively. The coefficient of variation indicates that there is 59.63% fluctuation in the variable and there is only 40.37% consistency in DPS.

In case of BOK, the shareholder are enjoying higher amount of cash DPS in each fiscal year compared to the dividend of previous year. The DPS of BOK followed an increasing trend and ranged from Rs.5 in the fiscal year 2002/03 to Rs.20 in the fiscal year 2006/07. The average DPS of this bank is Rs.13.60, standard deviation is 5.46 and coefficient of variation is 40.17 percent.

In conclusion, the average dividend per share paid by EBL (Rs.15) is comparatively higher than the average dividend per share of BOK (13.60). So, EBL is comparatively more successful to create the positive attitudes of shareholders towards the bank. It consequently helps to increase the market value of shares and also helps to indicate the better performance of the bank's management. However, the increasing trend adopted by BOK in paying dividend and high consistency in dividend payment (40.17%) compared to EBL (59.63%) indicate that there is good prospect of high dividend in BOK as well.

Figure 4.2
Dividend Per Share



4.3 Bonus Share Dividend (DP)

The bonus share dividend indicates the number of bonus share distributed for holding a single share. The bonus share dividend equivalent to Rupees of both EBL and BOK is presented in the following Table 4.3.

Table 4.3

Bonus Share Dividend

Year	EBL	BOK
2002/03	0	0
2003/04	0	0
2004/05	20	0
2005/06	0	30
2006/07	30	0
Total	50	30
Average	10	6
S.D. (†)	12.65	12.00
C.V.	126.49	200.00

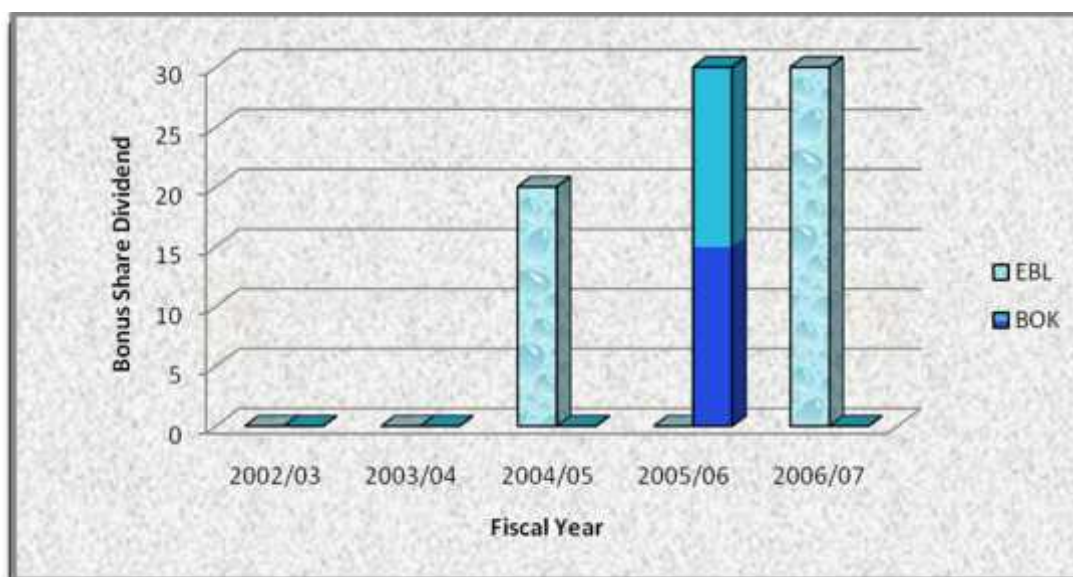
(Source: Annual report of EBL and BOK)

The table 4.3 shows that EBL paid bonus share only in two fiscal years viz, Rs. 20 in the fiscal year 2004/05 and Rs. 30 in the fiscal year 2006/07. EBL distributed an average bonus share of Rs.10 in the five year period. The standard deviation and coefficient of variation on the bonus share is Rs.12.65 and 126.49% respectively. The C.V. indicated that distribution of bonus share fluctuated by 126.49% in the periods taken for study.

Likewise, BOK distributed bonus share dividend Rs. 30 only in the fiscal year 2005/06. As a result the average bonus share of Rs.6 was paid by BOK in the five year period. The standard deviation is Rs.12 and coefficient of variation is 200%. The coefficient of variation shows that there is no standard policy of distributing bonus share as dividend in BOK.

Comparing the average bonus share dividend of EBL (Rs.12.65) and BOK (Rs.6), it can be considered that the shareholders of EBL enjoyed more bonus share than that of BOK.

Figure 4.3
Bonus Share Dividend



4.4 Dividend Payout Ratio (DPR)

Dividend payout ratio measures the percentage of dividend paid out of the net profit after tax. It also clears about the retained earning, since net profit is composed of dividend and retained earning only. Higher dividend payout ratio attracts the shareholders and consequently increases the market price of share. The dividend payout ratio of both banks is presented in the following Table 4.4.

Table 4.4
DPR Analysis

Fiscal Year	EBL			BOK		
	DPS	EPS	DPR	DPS	EPS	DPR
2002/03	20	29.90	66.89	5	17.72	28.22
2003/04	20	45.60	43.86	10	27.50	36.36
2004/05	0	54.20	0.00	15	30.10	49.83
2005/06	25	62.80	39.81	18	43.67	41.22
2006/07	10	78.40	12.76	20	43.50	45.98
Total			163.32			201.61
Average			32.66			40.32
S.D. (†)			23.71			7.55
C.V. %			72.59			18.74

(Source : Annual report of EBL and BOK)

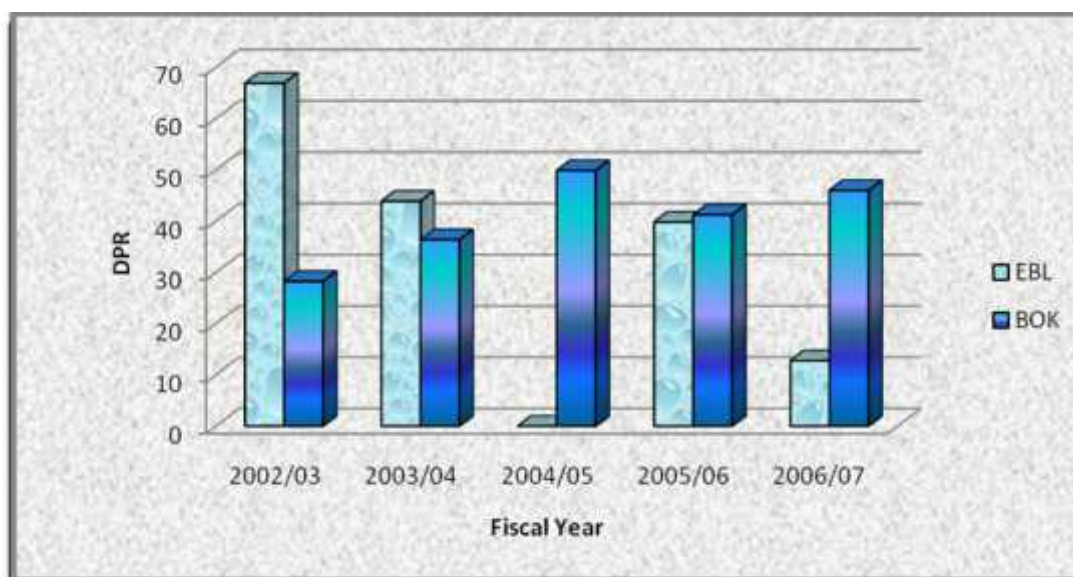
The table 4.4 shows that dividend payout ratio of EBL ranged from 0% in the fiscal year 2004/05, since no dividend distributed in that year, to 66.89% in the fiscal year 2002/03. The bank distributed almost two-third of its earning as a

dividend in the fiscal year 2002/03. The bank maintained an average DPR of 32.66% in the five fiscal years. The standard deviation of DPR is 23.71 and coefficient of variation is 72.59 percent. The coefficient of variation shows that the DPR fluctuated by 72.59% in the five year periods and there is high inconsistency in the DPR. Considering 0% DPR and 66.89% DPR in the fiscal year 2004/05 and 2002/03 respectively, it can be said that EBL does not have any benchmark to distribute dividend. Similarly, the DPR followed decreasing trend in the paid years, which indicates that the bank concentrated more on retained earning rather than paying dividend.

The DPR of BOK increased in each year except in the fiscal year 2005/06, when its DPR followed a decrease (8.61%) compared to the DPR of previous year 2004/05 (49.83%). The DPR of BOK ranged from 28.22% in the fiscal year 2002/03 to 49.83% in the fiscal year 2004/05. However, BOK maintained an average DPR of 40.32% during the five year period, which clearly indicated BOK gave more effort in retaining its existing shareholder and attracting potential shareholder toward it. The standard deviation and C.V. are also 7.55 and 18.74% respectively.

Thus, it can be concluded that BOK has more consistent DPR (C.V. 18.74%) than that of EBL (C.V. 72.59%) and also BOK's DPR is higher than that of EBL. Looking the average DPR (40.32%) of BOK, it can be said that BOK became more successful to satisfy its shareholder than EBL.

Figure 4.4
Dividend Payout Ratio



4.5 Price Earning Ratio (P/E Ratio)

Price Earning Ratio is the ratio between market price per share and earning per share. It indicates the payment by the investors in the market for per rupee of earning in the company. The price earning ratio of both banks for the period taken for study is presented in the following Table 4.5.

Table 4.5
Price Earning Ratio

Fiscal Year	EBL			BOK		
	MPS	EPS	P/E	MPS	EPS	P/E
2002/03	445	29.90	14.88	198	17.72	11.17
2003/04	680	45.60	14.91	295	27.50	10.73
2004/05	870	54.20	16.05	430	30.10	14.29
2005/06	1379	62.80	21.96	850	43.67	19.46
2006/07	2430	78.40	30.99	1375	43.50	31.61
Total			98.79			87.26
Average			19.76			17.45
S.D. (†)			6.20			7.73
C.V. %			31.37			44.32

(Source: Annual report of EBL and BOK)

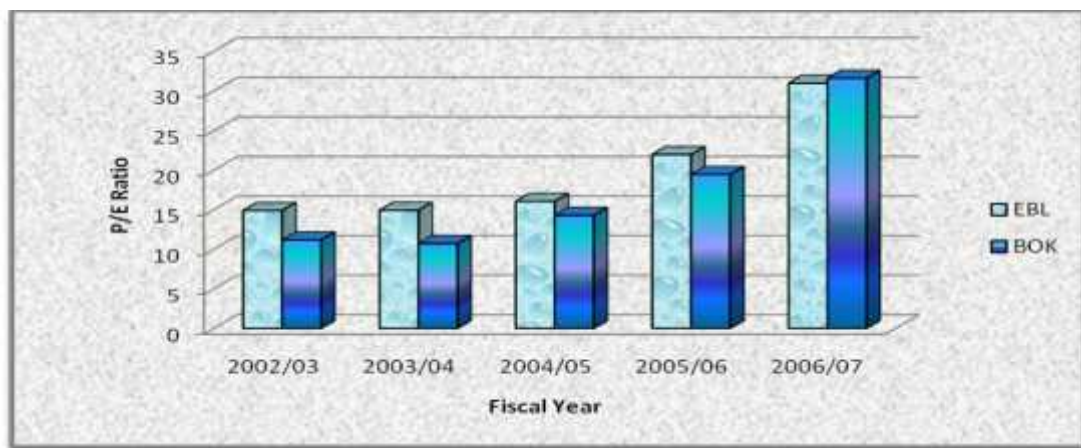
The table 4.5 depicts that the P/E Ratio of EBL ranged from 14.88 times in the fiscal year 2002/03 to 30.99 times in the fiscal year 2006/07. The P/E ratio of EBL followed an increasing trend in the five year period. However, EBL maintained an average 19.76 times P/E ratio in the five year period, which

indicates that the investors paid Rs. 19.76 for 1 rupee of earning in average. The standard deviation and coefficient of variation of the same bank in P/E ratio are 6.20 times and 31.37 percent respectively.

Likewise except in the fiscal year 2002/03, the P/E ratio of BOK also followed increasing trend. The P/E ratio of BOK in the base year was 11.27 times and decreased to 10.73 times in the fiscal year 2003/04 and then followed increasing trend and finally reached to 31.61 times in the fiscal year 2006/07. BOK maintained an average P/E ratio of 17.45 times in the five year period taken for research, which clearly indicates that the shareholders of BOK paid Rs. 17.45 to generate 1 rupee of earning. The standard deviation and the coefficient of variation are 7.73 and 44.32% respectively. The C.V. shows that there is more fluctuation in P/E ratio.

Comparing the P/E ratio of two banks, it can be considered that the investors of BOK paid less amount of Rs. 2.31 to gain 1 rupee of earning. However, the P/E ratio of BOK fluctuated more by 44.32% compared to P/E ratio of EBL in these periods.

Figure 4.5
Price Earning Ratio



4.6 Earning Yield Ratio (EY)

It measures the earning in relation to market value of share. It gives some idea of how much an investor might get for his money. The share with higher earnings yield is worth buying. Earning yield is informative to compare the

market share prices of stocks in the secondary market. The Earning Yield Ratio (EY) of EBL and BOK is presented in the following Figure 4.6.

Table 4.6
EY Analysis

Fiscal Year	EBL			BOK		
	EPS	MPS	EY	EPS	MPS	EY
2002/03	29.90	445	6.72	17.72	198	8.95
2003/04	45.60	680	6.71	27.50	295	9.32
2004/05	54.20	870	6.23	30.10	430	7.00
2005/06	62.80	1379	4.55	43.67	850	5.14
2006/07	78.40	2430	3.23	43.50	1375	3.16
Total			27.44			33.57
Average			5.49			6.71
S.D. (†)			1.38			2.32
C.V. %			25.17			34.60

(Source: Annual report of EBL and BOK)

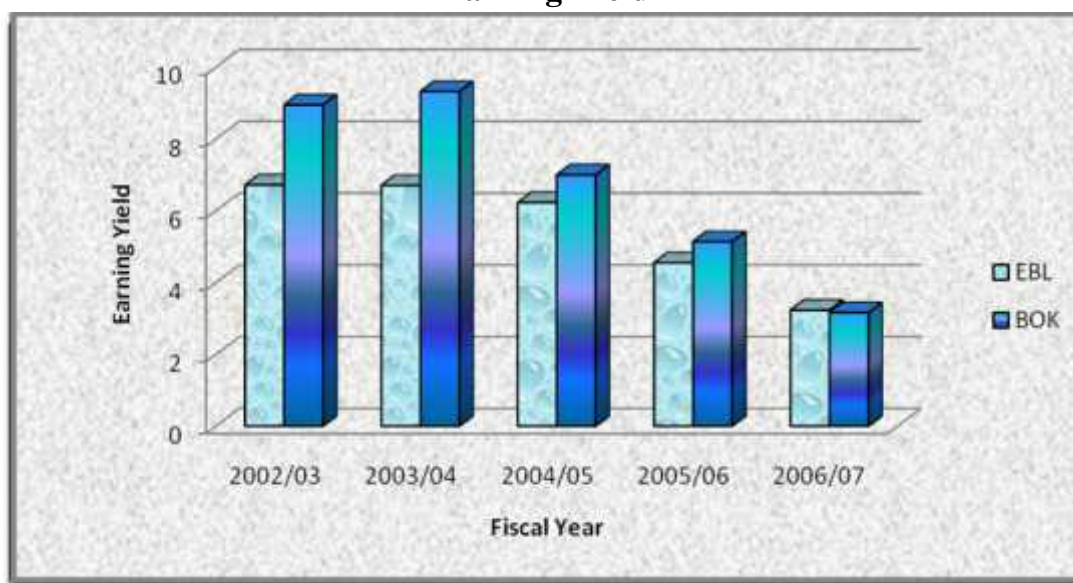
The relationship between earning per share and market price per share of two banks of different years are exhibited in the above table. The main reason behind such kind of tabulation is to point to the percentage relationship between EPS and MPS so as to illustrate the earning yield of the concerned banks, which may be a reliable tool to calculate the real value of the dividend as compared with the current market value of each share.

The table 4.6 depicts that the earning yield ratio of EBL is in decreasing in order. The earning yield decrease from 6.72% in the fiscal year 2002/03 to 3.23% in the fiscal year 2006/07. The average earning yield ratio of that bank is 5.49%, which is higher than the earning yield ratio of the last two year and is lower than the earning yield ratio of the remaining years. The standard deviation is 1.38 and the coefficient of variation is 25.17% respectively. The coefficient of variation indicates that there is 25.17% fluctuation in the EY of EBL. Similarly, the average EY of EBL indicates that only 5.49% of MPS is converted to EPS in the five year period. Although the EPS of EBL followed increased trend, the EY ratio indicates that the proportionate increase in EPS is lower than the proportionate increase in MPS, which means that the investor is paying more in the market to gain one rupee earning in each fiscal year.

Similarly, the earning yield ratio of BOK also followed decreasing trend except in the fiscal year 2003/04, where the EY raised to 9.32%. The EY ratio of BOK in the fiscal year 2002/03 is 8.95% and decreased to 3.16% in the fiscal year 2006/07. The average earning yield ratio is 6.71%, standard deviation is 2.32 and coefficient of variation is 34.60%. The average EY implies that EPS of BOK represents only 6.71% of MPS in the five year period.

Comparing the average earning yield ratio of EBL (5.49%) and that of BOK (6.71%), it can be considered that that BOK is more efficient in earning by 1.22% on the basis of market price of share.

Figure4.6
Earning Yield



4.7 Dividend Yield Ratio (DY)

Dividend yield is a percentage of dividends per share on market price per share. It shows that how much is the dividend per share on market price per share. The dividend yield ratio of EBL and BOK during the five year period is presented in the following Table 4.7.

Table 4.7
DY Analysis

Fiscal	EBL	BOK
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Year	DPS	MPS	DY	DPS	MPS	DY
2002/03	20	445	4.49	5	198	2.53
2003/04	20	680	2.94	10	295	3.39
2004/05	0	870	0.00	15	430	3.49
2005/06	25	1379	1.81	18	850	2.12
2006/07	10	2430	0.41	20	1375	1.45
Total			9.65			12.98
Average			1.93			2.60
S.D. (†)			1.65			0.77
C.V. %			85.53			29.71

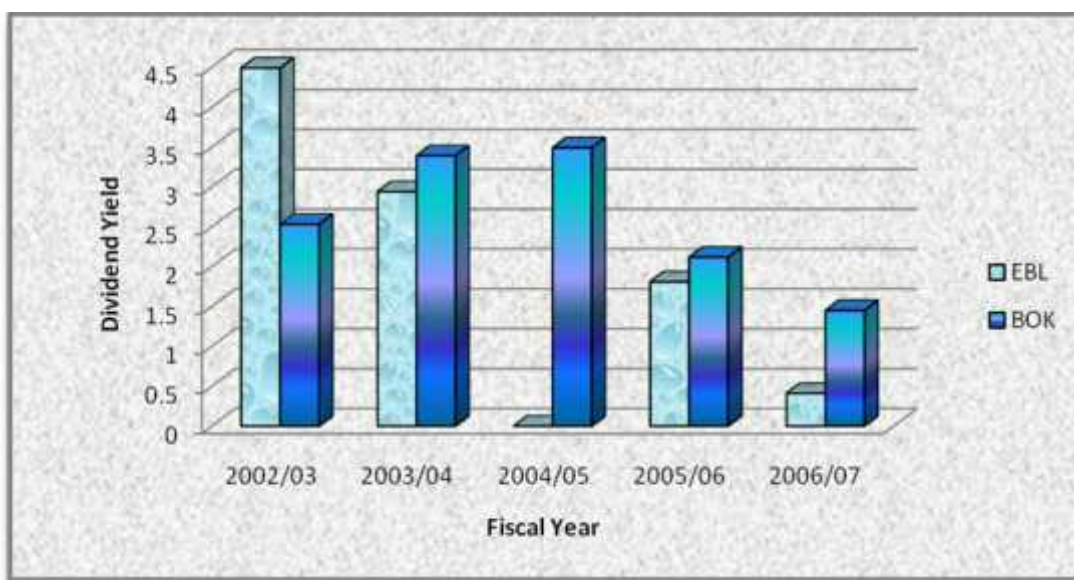
(Source: Annual report of EBL and BOK)

The above table depicts that the dividend yield ratio of EBL ranged from 0% in the fiscal year 2004/05, when no dividend paid, to 0.41% in the fiscal year 2006/07. The dividend yield ratio followed decreasing trend, looking the dividend paid years. The DY fall from 4.49% in the fiscal year 2002/03 to 0.41% in the fiscal year 2006/07. The average dividend yield of EBL during the five year period is only 1.93% and the standard deviation & C.V. are 1.65 and 85.53% respectively. The average dividend yield of EBL indicated that the shareholders are paid dividend of only 1.65% of the market price, they invested per share.

Similarly, the dividend yield of BOK followed fluctuating trend. The DY ranged from 1.45% in the fiscal year 2006/07 to 3.49% in the fiscal year 2004/05. BOK maintained an average dividend yield of 2.60%, which indicated that the shareholder of BOK got Rs.2.60 dividend for Rs.100 investment per share in the market. Likewise, standard deviation and C.V. of DY in BOK are 0.77 and 29.71% respectively.

Comparing the average dividend of BOK (2.60%) and EBL (1.93%), it can be considered that the shareholders of BOK got more percentage of the market price they paid for a share as dividend in return.

Figure 4.7
Dividend Yield



4.8 Market Value per Share (MPS) to Book value per share (BVPS) Ratio

This ratio indicates the price that the market is paying for the share that is reported from the net worth of the banks. The market price per share to book value per share of both banks is presented in the following Table 4.8.

Table 4.8
Analysis of MPS to BVPS Ratio

Fiscal Year	EBL			BOK		
	MPS	BVPS	Ratio	MPS	BVPS	Ratio
2002/03	445	150.10	2.96	198	192.52	1.03
2003/04	680	171.52	3.96	295	218.38	1.35
2004/05	870	219.87	3.96	430	213.60	2.01
2005/06	1379	217.67	6.34	850	230.67	3.68
2006/07	2430	292.75	8.30	1375	162.81	8.45
Total			25.52			16.52
Average			5.10			3.30
S.D. (†)			1.95			2.73
C.V. %			38.15			82.65

(Source: Annual report of EBL and BOK)

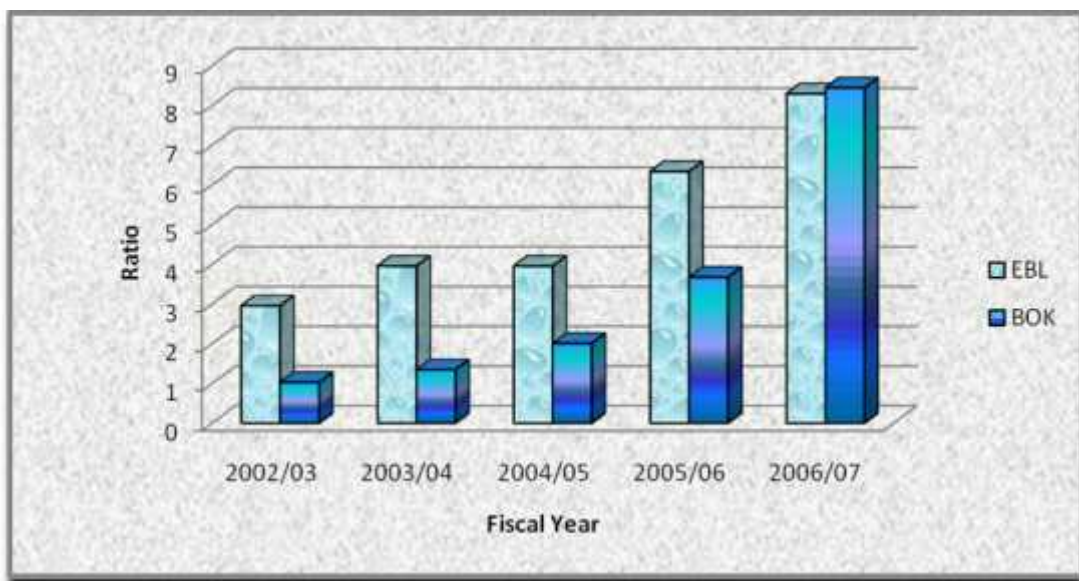
The table 4.8 shows that the ratio of market value per share (MPS) to book value per share (BVPS) of EBL is in ascending order in the five year periods. The ratio increased from 2.96 times in the fiscal year 2002/03 to 8.30 times in the fiscal year 2006/07. It means that the investor paid Rs. 2.96 in the market for Re. 1 book value of the share in the fiscal year 2002/03 and Rs. 8.30 in the market for Re. 1 book value of the share 2006/07. The average MPS to BVPS in

the five year period is 5.10 times, standard deviation is 1.95 and C.V. is 38.15%. In average, investor paid 5.10 times of the book value per share in the market to possess a single share.

Likewise, the market price per share to book value per share of BOK increased in each fiscal year. The ratio ranged from 1.03 times to 8.45 times in the fiscal year 2002/03 and 2006/07 respectively. The average ratio of BOK is 3.30 times, standard deviation is 2.73 and coefficient of variation is 82.65 percent. In the five year period, the shareholders paid 3.30 times more than the book value per share to acquire a single share in market value.

Figure 4.8

Market price per Share to Book value per Share



4.9 Simple Correlation and Regression Analysis

To find the relationship of dividend with other determinants of share price the Karl Pearson's correlation coefficient and simple regression lines have been analyzed.

4.9.1 Dividend per Share (DPS) and Earning Per Share (EPS)

4.9.1.1 Correlation between DPS and EPS

The correlation coefficient between DPS and EPS as calculated in Appendix I is summarized below.

Table 4.9

Correlation Coefficient between DPS and EPS

Banks	r	Relationship	r²	P.E.	6 P.E.	Remarks
EBL	-0.2741	-ve (Indirect)	0.0751	0.2790	1.6739	Insignificant
BOK	0.9615	+ve (direct)	0.9245	0.0228	0.1366	Significant

(Source: Appendix I)

The Table 4.9 helps to depict the relationship between Earning Per Share (EPS) and Dividend Per Share (DPS) of EBL and BOK.

The correlation coefficient (r) between EPS and DPS of EBL is -0.2741 which indicates the negative relationship between EPS and DPS. It means that the DPS increases with the decrease in EPS of EBL. Coefficient of determination is the measure of the degree of linear association or correlation between two variables. The value of r² of EBL is 0.0751, which indicates that 7.51% of variation is explained in the dependent variable DPS due to the change in the value of independent variable EPS. However, the lower 'r' value (-0.2741) than 6 P.E. (1.6739) indicates that the relationship between EPS and DPS is insignificant and reveals that it is not necessary that DPS always declines with the increase in EPS.

Likewise, the relationship between EPS and DPS of BOK is positive, 0.9615, and the degree of correlation coefficient is high. The coefficient of determination between EPS and DPS is 0.9245, which indicates that the variations in the DPS explain 92.45% due to change in the value of EPS. The probable error indicates that the relationship between EPS and DPS of BOK is significant as the value of 'r' (0.9615) is greater than 6 P.E. (0.1366), which indicates that DPS always increases with the increase in EPS.

4.9.1.2 Regression Analysis: Dividend per Share (DPS) on Earning Per Share (EPS)

The simple regression equation of DPS on EPS calculated in the Appendix I is:

$$Y = a + b X$$

$$DPS_{EBL} = 23.16 - 0.1507 \times EPS_{EBL}$$

$$DPS_{BOK} = -3.56 + 0.5279 \times EPS_{BOK}$$

The regression variable and t-value obtained is summarized in the following Table 4.10.

Table 4.10
Regression Analysis of DPS on EPS

Banks	no. of observation (n)	Constant (a)	regression coefficient (b)	T value
EBL	5	23.16	-0.1507	-0.49
BOK	5	-3.56	0.5279	6.06

(Source: Appendix II)

The Table 4.10 depicts the output of simple regression analysis of DPS on EPS of the two banks viz. EBL and BOK. In case of EBL, beta coefficient is -0.1507, which indicates that a one rupee increase in EPS leads to an average Re. 0.1507 decrease in dependent variable DPS, holding the constant (a), 23.16, uniform. Also, the calculated value of t (-.049) is lower than the tabulated value of t (2.78) at 5% level of significance and 4 Degree of freedom, which indicates that the result is statistically insignificant.

In the case of BOK, the beta coefficient is 0.5279, which indicates a one-rupee increase in EPS leads to an average Re.0.5279 increase in DPS, if the constant (a), -3.56, remains same. Since calculated t-value (6.06) of BOK is higher than the tabulated value of t (2.78) at 5% level of significance, the result is statistically significant.

4. 9.2 Average Stock Price (MPS) and Dividend per Share (DPS)

4.9.2.1 Correlation between MPS and DPS

The correlation between MPS and DPS and the probable error calculated in *Appendix I* is summarized in the below Table 4.11.

Table 4.11
Correlation Coefficient between DPS and EPS

Banks	r	Relationship	r²	P.E.	6 P.E.	Remarks
EBL	-0.1834	-ve (indirect)	0.0336	0.2915	1.7490	Insignificant
BOK	0.8752	+ve (direct)	0.7660	0.0706	0.4236	Significant

(Source: Appendix II)

The Table 4.11 reveals the relationship between dividend per share (DPS) and market price of stock (MPS). Coefficients of correlation of EBL and BOK are -0.1834 and 0.8752 respectively. The coefficient of correlation between DPS and MPS of EBL and BOK indicates the negative correlation and higher degree of positive correlation respectively. However, there is no significant relationship between MPS and DPS of EBL since the 'r' (-0.1834) is lower than the 6 P.E. (1.7490). In case of BOK, since the value of 'r' (0.8752) is greater than 6 P.E. (0.4236), there is significant relationship between MPS and DPS, which means MPS increases with the increase on DPS.

4.9.2.2 Regression Analysis : Average Stock Price (MPS) on Dividend Per Share (DPS)

Let the dependent variable MPS is denoted by Y and independent variable DPS is denoted by X, then the regression equation of MPS on DPS is given by:
(Appendix I)

$$Y = a + b X$$

$$MPS_{EBL} = 1377.74 - 14.46 \times DPS_{EBL}$$

$$MPS_{BOK} = -316.31 + 69.55 \times DPS_{BOK}$$

Table 4.12
Regression Analysis of MPS on DPS

Banks	no. of observation (n)	Constant (a)	Regression coefficient (b)	T-value
EBL	5	1377.74	-14.46	-0.32
BOK	5	-316.31	69.55	3.13

(Source: Appendix I)

The Table 4.12 depicts the major output of simple regression analysis of average market price per share (MPS) on dividend per share (DPS) of the concerned banks.

As far as the regression of MPS and DPS is concerned, the regression coefficient of EBL and BOK are -14.46 and 69.55 respectively. It indicates that a one-rupee increase in DPS leads to an average of Rs. 14.46 decrease in MPS of EBL and Rs.69.55 increase in MPS of BOK, if the other variable remains constant. The test of t-statistics aid to conclude that in EBL the relationship between MPS and DPS is insignificant, since the calculated value of t (-0.32) is lower than tabulated value of t (2.78) and in BOK the results are statistically significant, since the calculated t-value (3.13) is higher than the tabulated t-value (2.78) at 5% level of significance on 4 degree of freedom.

4.9.3 Book value per Share (BVPS) and Dividend Per Share (DPS)

4.9.3.1 Correlation between BVPS and DPS

The correlation coefficient between BVPS and DPS and the probable error is presented in the following Table 4.13.

Table 4.13
Correlation between BVPS and DPS

Banks	r	Relationship	r ²	P.E.	6 P.E.	Remarks
EBL	-0.4446	-ve (indirect)	0.1977	0.2420	1.4521	Insignificant

BOK	-0.1320	-ve (indirect)	0.0174	0.2964	1.7784	Insignificant
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(Source: Appendix I)

The Table 4.13 depicts the relationship between dividend per share (DPS) and book value per share (BVPS) of the two concerned banks. Coefficient of correlation between DPS and BVPS of EBL and BOK are -0.4446 and -0.1320 respectively. EBL has negative correlation between DPS and BVPS, which means that BVPS decreases with the increase in DPS. Likewise the negative correlation between BVPS and DPS of BOK implies that BVPS decreases with the increase in DPS. The probable error of EBL also shows that the relationship between BVPS and DPS is insignificant, since the 'r' (-0.4446) is lower than the 6 P.E. (1.4521) and the relationship between DPS and BVPS of BOK is also insignificant, since the value of 'r' (-0.1320) is lower than the 6 P.E. (1.7784).

4.9.3.2 Regression Analysis: Book value per Share (BVPS) on Dividend per Share (DPS)

Let BVPS be denoted by Y and DPS be denoted by X, then the regression line of BVPS (Y) on DPS (X) is given by: (Appendix I)

$$Y = a + b X$$

$$BVPS_{EBL} = 247.02 - 2.4425 \times DPS_{EBL}$$

$$BVPS_{BOK} = 211.42 - 0.5755 \times DPS_{BOK}$$

Table 4.14
Regression Analysis of DPS on BVPS

Banks	No. of observation (n)	Constant (a)	Regression coefficient (b)	T-value
EBL	5	247.02	-2.4425	-0.86
BOK	5	211.42	-0.5755	-0.23

(Source: Appendix I)

With respect to the above regression result of Book value per Share (BVPS) on dividend per share (DPS), beta coefficients in both banks, EBL (-2.4425) and (-0.5755), are negative. The beta coefficient of EBL (-2.4425) indicates that 1 rupee increase in Dividend per share leads to Re. 2.4425 decrease in Book

value per Share. Hence the relationship between BVPS and DPS of EBL is inverse. Similarly, the beta coefficient of BOK (-0.5755) implies that 1 rupee increase in DPS yields to 0.5755 decrease in BVPS. Also, the calculated t-value (-0.86) shows that the relationship between BVPS and DPS of EBL is insignificant and the calculated t-value of BOK (-0.23) proves that the relationship between BVPS and DPS is also insignificant as the calculated value of 't' is lower than the tabulated 't' (2.78) at 5 percent level of significance and 4 degree of freedom.

4.9.4 Earning Yield (EY) and Dividend Yield (DY)

4.9.4.1 Correlation between EY and DY

The correlation between DY and EY and the probable error determined in Appendix III is summarized in the below Table 4.15.

Table 4.15
Correlation between EY and DY

Banks	r	Relationship	r²	P.E.	6 P.E.	Remarks
EBL	0.5702	+ve (direct)	0.3252	0.2036	1.2214	Insignificant
BOK	0.7814	+ve (direct)	0.6106	0.1175	0.7048	Significant

(Source: Appendix I)

The Table 4.15 depicts the relationship between earning yield (EY) and dividend yield (DY) of two concerned banks. According to this table, the correlation coefficients between DY and EY of EBL and BOK are 0.5702 and 0.7814 respectively. In case of EBL, it has a low positive correlation between the two variables. And coefficient of determination (r^2) indicates that 32.52% variation is explained in dividend yield due to change in the value of earning yield. However, the Probable Error (0.2036) shows that there is insignificant relationship between the DY and EY of EBL because the correlation coefficient 'r' (0.5702) is lower than 6 P.E. (1.2214).

The coefficient of correlation between earning yield and dividend yield of BOK (0.7814) shows the positive correlation between the variables, which means that DY increases with the increase in EY. And coefficient of

determination r^2 indicates that 61.06% variation is explained in dividend yield due to the change in the value of earning yield. Since correlation coefficient 'r' of BOK (0.7814) is higher than 6 P.E. (0.7048), there is significant relationship between the two variables.

4.9.4.2 Regression Analysis : Dividend yield (DY) on Earning yield (EY)

Let dividend yield be denoted by Y and earning yield be denoted by X, then the regression line of dividend yield on earning yield is given by;

$$\begin{aligned}
 Y &= a + b X \\
 DY_{EBL} &= -1.81 + 0.6814 \times EY_{EBL} \\
 DY_{BOK} &= 0.8543 + 0.2594 \times EY_{BOK}
 \end{aligned}$$

Table 4.16

Regression Analysis of DY on EY

Banks	no. of observation (n)	constant (a)	Regression coefficient (b)	T-value
EBL	5	1.81	0.6814	1.20
BOK	5	0.8543	0.2594	2.17

(Source: Appendix I)

The table 4.16 depicts the major output of simple regression analysis of Dividend Yield (DY) on Earning Yield (EY) of the concerned banks.

With respect to the above regression result of dividend yield (DY) in earning yield (EY), in case of EBL beta coefficient is 0.6814, which means that a one rupee increase in earning yield leads to an average of about Rs. 0.6814 increase in the dividend yield holding other variables constant. However, the result is not statistically significant at 5% level of significance because the computed value of 't' (1.20) is lower than the tabulated value of 't' (2.78).

While in case of BOK, beta coefficient is 0.2594, which indicates that a one rupee increase in earning yield leads to an average of about Rs.2594 increase in the dividend yield holding other variables constant. This result is also

statistically insignificant at 5% level of significance because the computed value of 't' (2.17) is higher than the tabulated value of t (2.78).

4.9.5 Market Price Per Share (MPS) and Dividend Payout Ratio (DPR)

4.9.5.1 Correlation between MPS and DPR

Let 'r' be the correlation coefficient between MPS and DPR and P.E. be the probable error.

Table 4.17
Correlation between MPS and DPR

Banks	r	Relationship	r²	P.E.	6 P.E.	Remarks
EBL	-0.5273	-ve (indirect)	0.2781	0.2178	1.3066	Insignificant
BOK	0.5529	+ve (direct)	0.3057	0.2094	1.2566	Insignificant

(Source: Appendix I)

As shown in Table 4.17, the correlation coefficient between dividend pay out ratio (DPR) and market price per share of EBL and BOK are -0.5273 and 0.5529 respectively, which indicates negative relationship between the two variables of EBL and a moderate degree of positive relationship between the variables of BOK. Coefficient of determination (r^2) of EBL is 0.2781, which shows DPR of EBL explains 27.81% of variations in the MPS. Likewise, according to the same table, coefficient of determination (r^2) of BOK is 0.3057, which explains that the variation in the DPR explains 30.57% of variations in MPS.

Since, r of EBL (-0.5273) is lower than 6 P.E. (1.3066), the relationship between DPR and MPS is insignificant, which means that the increase in DPR does not necessarily mean the decrease in MPS. Similarly, r of BOK (0.5529) is lower than 6 P.E (1.2566), which also indicates that there is insignificant relationship between DPR and MPS.

4.9.5.2 Regression Analysis : Market Price Per Share (MPS) on Dividend Payout Ratio (DPR)

Let MPS be denoted by Y and DPR be denoted by X, then the regression line of Y on X is given by:

$$Y = a + b X$$

$$MPS_{EBL} = 1673.10 - 15.68 \times DPR_{EBL}$$

$$MPS_{BOK} = -651.44 + 31.77 \times DPR_{BOK}$$

Table 4.18

Regression Analysis of MPS on DPR

Banks	no. of observation (n)	constant (a)	Regression coefficient (b)	T-value
EBL	5	1673.10	-15.68	-1.07
BOK	5	-651.44	31.77	1.15

(Source: Appendix I)

The Table 4.18 depicts the linear relationship between stock price (MPS) and dividend pay out ratio (DPR) of concerned banks. In case of EBL, beta coefficient is -15.68, which indicates that a one percent increase in dividend payout ratio (DPR) leads to an average Rs. 15.68 decrease in market price per share (MPS), all other things being same. However, the calculated 't' value (-1.07) is lower than the tabulated 't' value (2.78) at 5% level of significance and 4 d.f., which means that there is insignificant relationship between DPR and MPS of EBL.

Similarly, in case of BOK, beta coefficient is 31.77, which indicates that a one percent increase in DPR leads to an average Rs. 31.77 increase in market price per share, other variables remaining constant. But the calculated $t_{0.05}$ (1.15), which is lower than the tabulated $t_{0.05}$ (2.78), shows that the relationship between DPR and MPS of BOK is insignificant.

4.10 Market Price Per Share (MPS) and Earning Per Share (EPS) and Dividend Per Share (DPS)

4.10.1 Multiple Correlations between MPS, EPS and DPS.

Let correlation between MPS and DPS be denoted by r_{12} , DPS and EPS be denoted by r_{23} and MPS and EPS be denoted by r_{13} . Then the multiple correlation coefficient of MPS on DPS and EPS is given by; (*Appendix II*)

$$R_{1.23} = \sqrt{\frac{r_{12}^2 + r_{13}^2 - 2 r_{12} r_{23} r_{13}}{1 - r_{23}^2}}$$

$$R_{\text{MPS,DPS EPS (EBL)}} = 0.9464$$

$$R_{\text{MPS,DPS EPS (BOK)}} = 0.8919$$

Table 4.19

Multiple Correlations between MPS, EPS and DPS

Banks	R	Relationship	R²	P.E.	6 P.E.	Remarks
EBL	0.9464	+ve (Direct)	0.8957	0.0315	0.1887	Significant
BOK	0.8919	+ ve (Direct)	0.7955	0.0617	0.3702	Significant

(*Source: Appendix II*)

The above Table 4.19 shows the multiple correlation between market price per share (MPS) and dividend per share (DPS) and earning per share (EPS) of two concerned banks during the year covered for research. The multiple correlation coefficients (R) between MPS, DPS and EPS of EBL and BOK are 0.9464 and 0.8919 respectively, which show the high degree of positive relationship between these variables of both the banks.

The coefficient of multiple determination (R²) of EBL is 0.8957, which is slightly higher than that of BOK (i.e. 0.7955). It shows that, in case of EBL, 89.57% of variation in dependent variable (MPS) is explained by the variation in independent variables (EPS and DPS). Similarly, 79.55% variation in dependent variable (MPS) of BOK is explained by the variation in independent variables (DPS and EPS).

To measure the significance of the relationship between MPS, EPS and DPS of the two concerned banks, it would be more preferable to calculate the probable error of correlation coefficient. The same table depicts that R of both banks is greater than 6 P.E of corresponding banks. So, it can be concluded that the relationship between MPS, EPS and DPS is significant in both banks. It all indicates that market price per share depends upon dividend payments and earning per share.

4.10.2 Multiple Regression Equation : MPS on DPS and EPS

Let MPS, DPS and EPS be denoted by X_1 , X_2 and X_3 respectively. Then the multiple regression equation of MPS on DPS and EPS is given by;

$$X_1 = a + b_1 X_2 + b_2 X_3$$

$$MPS_{EBL} = -1091.22 + 5.51 DPS_{EBL} + 40.04 EPS_{EBL}$$

$$MPS_{BOK} = -552.91 + 21.81 DPS_{EBL} + 27.26 EPS_{EBL}$$

Table 4.20

Multiple Regression Line of MPS on DPS and EPS

Banks	No. of year	Constant (a)	Regression Coefficient (b)	
			b_1	b_2
EBL	5	-1091.22	5.51	40.04
BOK	5	-552.91	21.81	27.26

(Source: Appendix II)

The above table represents the linear relationship between MPS, with DPS and EPS of two concerned banks. The constant (a) is negative in EBL (-1091.22) and BOK (-552.91). In case of EBL, the beta coefficient of DPS and EPS are 5.51 and 40.04 respectively. It indicates that a one-rupee increase in DPS leads to Rs.5.51 increase in MPS and one rupee increase in EPS leads to an average about Rs.40.04 increase in MPS.

On the other hand, in case of BOK, the regression coefficients of DPS and EPS are 21.81 and 27.26 respectively, which indicates that a one-rupee increase in DPS causes Rs. 21.81 increase in MPS and one-rupee increase in EPS leads to

an average about Rs. 27.26 increase in MPS. Hence, it can be concluded that DPS and EPS has direct influence on MPS of BOK.

4.11 Trend Analysis

The trend analysis aids to predict the future value on the basis of the past years. To know the DPS and DPR of the concerned banks the trend analysis has been used.

4.11.1 Trend Analysis of DPS

Let Year (X) 1, 2, 3, 4 and 5 denotes fiscal year 2002/03, 2003/04, 2004/05, 2005/06 and 2006/07 respectively. Then regression line of DPS (Y) on year is given by;

$$Y = a + b X$$

$$DPS_{EBL} = 19.50 - 1.50 X$$

$$DPS_{BOK} = 2.20 + 3.80 X$$

The trend value of DPS calculated from this regression equation is presented in the following table.

Table 4.21

Trend Analysis of DPS

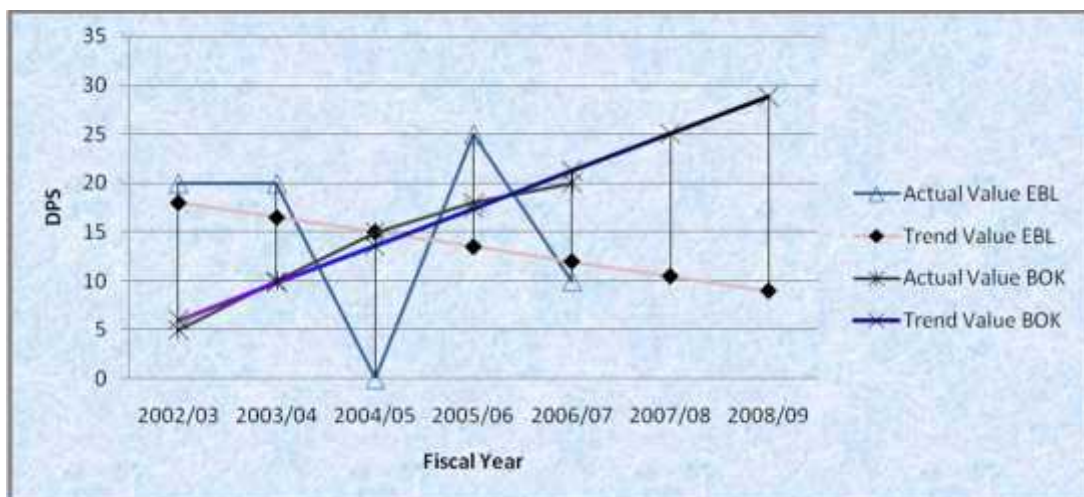
Fiscal Year	EBL		BOK	
	Actual DPS	Trend DPS	Actual DPS	Trend DPS
2002/03	20	18.00	5	6.00
2003/04	20	16.50	10	9.80
2004/05	0	15.00	15	13.60
2005/06	25	13.50	18	17.40
2006/07	10	12.00	20	21.20
2007/08		10.50		25.00
2008/09		9.00		28.80

(Source: Appendix III)

The table 4.21 shows that the trend DPS of EBL follows decreasing trend. The table depicts that the DPS of EBL in the fiscal year 2007/08 and 2008/09 will be Rs. 10.50 and Rs. 9.00 respectively. Likewise, the table shows that the trend DPS of BOK follows increasing trend. The estimated value of DPS for the fiscal year 2007/08 and 2008/09 will be Rs. 25.00 and Rs. 28.80 respectively.

On the basis of predicted value, BOK has good prospects for shareholders on the basis of dividend per share.

Figure 4.9
Trend Value of DPS



4.11.2 Trend Analysis of DPR

Let X denotes the fiscal year and Y denotes the DPR. Then regression line of DPR (Y) on year is given by;

$$Y = a + b X$$

$$DPR_{EBL} = 19.50 - 1.50 X$$

$$DPR_{BOK} = 2.20 + 3.80 X$$

The trend value of DPR calculated from this regression equation is presented in the following table.

Table 4.22
Trend Analysis of DPR

Fiscal Year	EBL		BOK	
	Actual DPR	Trend DPR	Actual DPR	Trend DPR
2002/03	66.89	55.13	28.22	32.25
2003/04	43.86	43.90	36.36	36.29
2004/05	0.00	32.67	49.83	40.33

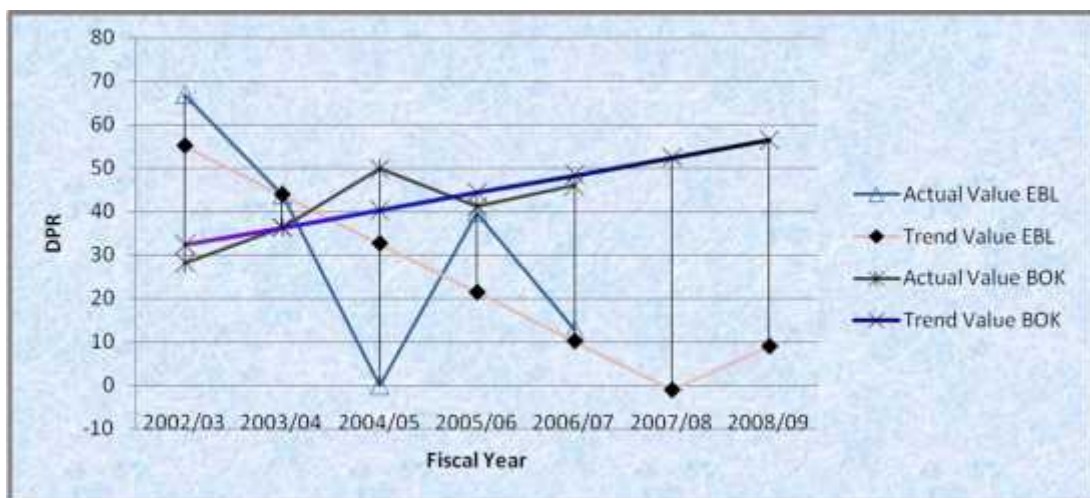
2005/06	39.81	21.44	41.22	44.37
2006/07	12.76	10.21	45.98	48.41
2007/08		-1.02		52.45
2008/09		-12.25		56.49

(Source: Appendix III)

The table 4.22 shows that there is negative relationship between DPR and year of EBL. In each fiscal year the DPR of EBL decreases by the multiple of 1.50 percent. Since, the DPR is negative in the fiscal year 2007/08 and 2008/09, EBL will pay no dividend in these years.

Similarly, the dividend payout ratio of BOK increases with the multiple of 3.80% in each fiscal year. The DPR of BOK in the fiscal year 2007/08 and 2008/09 will be 52.45% and 56.49% respectively.

Figure 4.10
Trend Value of DPR



4.12 Major Findings of the Study

On the basis of the analysis of data, the following major findings have been found.

- EPS analysis shows that the average EPS of EBL (Rs.54.18) is greater than the average EPS of BOK (Rs.32.50). The EBL earned higher

earning per share in comparison with the EBL bank. Similarly, the C.V. analysis of EPS in EBL (30.04%) is more consistent as compared to that of BOK (30.62%).

- b. EBL distributed Rs.15 as DPS in average, while BOK distributed an average DPS of Rs.13.60 during the period taken for research. However, there is more consistent in DPS of BOK (c.v. 40.17%) as compared to the dividend distribution of EBL (c.v. 59.63%).
- c. EBL distributed bonus share dividend only in two fiscal years taken for research. The average bonus share equivalent to Rs.10 per share has been distributed during the period. While, BOK distributed bonus share only in the fiscal year 2005/06 equivalent to Rs.30 per share. Therefore there is no standard bonus share dividend policy in both BOK and EBL.
- d. The DPR ratio shows that EBL provided an average 32.66% of its EPS as dividend which is comparatively low compared to the dividend payout ratio of BOK (40.32%). EBL focused more on retaining profit for internal financing purpose, whereas BOK focused more on retaining shareholders through providing more dividends.
- e. The P/E ratio shows that MPS of EBL is almost 19.76 times greater than its average EPS, whereas the MPS of BOK is almost 17.45 times higher than EPS. This means that the shareholder of EBL invests Rs.19.76 and that of BOK invests Rs.17.45 to achieve one rupee earning per share.
- f. The dividend yield ratio shows that only 1.93% of the average market price of EBL was provided as dividend during the period taken for study, whereas 2.60% of the MPS of BOK was provided as dividend. Hence the shareholders of BOK enjoyed more dividend percent compared to the shareholders of EBL on the basis of MPS. Also, the MPS is 5.10 times greater than BVPS of EBL, while the MPS of BOK is 3.30 times higher than the BVPS.
- g. In case of EBL, the correlation of DPS with EPS, MPS and BVPS is negative and the results are also insignificant. However, the correlation between EY and DY is positive and but statistically insignificant.

Likewise, the correlation between MPS and DPR is negative and the result is insignificant.

- h. But, in case of BOK, the correlation of DPS with EPS and MPS is positive and the relationship is significant but the correlation between DPS and MPS is negative and insignificant. However, the correlation between DY and EY is positive and significant.
- i. Likewise, the correlation between MPS and DPR of EBL is negative and the correlation between MPS and DPR is positive. However, the relationship between them in both banks is statistically insignificant.
- j. The estimated DPS on EBL for the fiscal year 2007/08 and 2008/09 will be Rs. 10.50 and Rs. 9.00 respectively. Similarly, the predicted DPS on BOK for the fiscal year 2007/08 and 2008/09 will be Rs.25.00 and Rs. 28.80 respectively.
- k. The estimated DPR of BOK for the fiscal year 2007/08 and 2008/09 will be 52.45% and 56.49% respectively. However, the DPR of EBL in the same period will be Nil.
- l. The multiple regression equation indicated that one rupee increase in DPS leads to Rs. 5.51 increase in MPS and one rupee increase in EPS yields Rs. 40.04 increase in MPS in EBL. Similarly, in BOK, one rupee increase in DPS explains Rs. 21.81 increase in MPS and one rupee increase in EPS results Rs. 27.26 increase in MPS of BOK.

CHAPTER V

SUMMARY CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Dividend policy decision is undoubtedly one of the three major decisions of financial management. It is right to say that dividend policy decision affects the operation and prosperity of a financial company because it has the power to influence other two decisions namely capital structure decision and investment decision. Basically an investor expects two types of return namely, capital gain and dividend, by investing in equity capital or ordinary share. So, payment of dividend to shareholders is an effective way to attract new investors and maintain present investors to invest in shares. So, it is justified to hold that a clearly defined and effectively managed dividend policy is required in all financial companies to fulfill the shareholders expectations with that of corporate growth from internally generated funds. So, the funds that could not be used due to lack of investment opportunities would be better to be distributed as dividend, since shareholders have investment opportunities elsewhere.

Considering time and resource constraints only two commercial banks namely BOK and EBL have been selected as sample banks in study to fulfill the objective of studying dividend policy decision and other factors related to dividend. The study period covers only last five fiscal years from 2002/03 to 2006/07. The available secondary data have been analyzed using various financial and statistical tools in this study. So, the reliability of the conclusions of this study is determined on the accuracy of secondary data.

The study is organized in five chapters, viz, i) Introduction, ii) Review of Literature, iii) Research Methodology, iv) Data Presentation and Analysis and v) Summary Conclusion and Recommendations.

5.2 Conclusion

On the basis of secondary data analysis, it can be concluded that EBL has higher earning capacity than BOK and paying more dividend in Rupees than that of BOK. However, on the basis of DPR, it can be considered that BOK is paying higher portion of its earning as dividend since the average DPR of BOK is higher than that of EBL. Likewise, both banks do not have benchmark of distributing bonus share as dividend. Similarly, the investors of BOK are investing fewer amounts in the market than that of EBL in order to gain per rupee earning. The dividend payout ratio shows that BOK has the policy of alluring its shareholders and EBL has the policy of retaining its earning for internal financing.

Average dividend yield indicates that BOK is providing more percentage of its market value per share than EBL. Similarly, average earning yield ratio of BOK is greater than that of EBL, which means BOK is more efficient to generate earning on the basis of market price. However, average market value per share to book value per share of EBL is greater than that of BOK. So, there is greater chance of higher capital gain to the shareholders of EBL.

The correlation of DPS of BOK with EPS, MPS is positive and significant whereas the correlation between DPS and BVPS is negative and insignificant and the correlation between DPR and MPS is positive but statistically insignificant. This means that DPS increases with the increase in EPS and, MPS increases with the increase in DPS. But, in case of EBL, the correlation of DPS with EPS, MPS and BVPS is negative and insignificant, whereas the correlation between EY and DY is positive but statistically insignificant. Similarly, the correlation between MPS and DPR is negative and insignificant. This implies that there is no significant relationship between DPS with EPS, MPS and BVPS of EBL.

Finally on the basis of secondary data, it can be concluded that EBL remained more successful than BOK in satisfying its shareholder through distributing

cash and bonus share dividend, generating higher amount of earning per share, maintaining higher market value of its share. However, BOK remained more generous in distributing dividend by providing high dividend payout ratio and keeping good relationship between DPS, EPS and MPS.

5.3 Recommendations

Based on major findings and conclusion drawn, the major are provided below hoping that these recommendations will certainly be proved milestone to overcome existing issues in this field.

- ❖ The bank should consider the existing conditions and expectations of shareholders while distributing dividends so that the distributed dividend should meet the interests or expectations of the shareholders as far as possible.
- ❖ The bank should study about the strategy to attract the ordinary or small or low level investors so that the interest or the expectation of shareholders will not be destroyed even the bank can't pay the dividend in some year.
- ❖ There should be certain program to improve the efficiency and reduce the government interference in daily affair. Similarly, the managers should be able to fulfill their duties and responsibilities and to protect the shareholder's interest but not for operation of company desired by themselves.
- ❖ Banks are playing on the public money. So in this regard, they are advised to have target rate of return (earnings) and target payout ratio that will help the banks to build good image in stock market and investors will be benefited on making investment decision.
- ❖ It would be better to fix the amount of dividend in the annual general meeting of shareholders. This is important not only from the point of view of adequate return to shareholders but also to generate stable and increasing

market value per share, long run survival of bank, efficient management and socially acceptable distribution of income.

- ❖ The banks should define their dividend strategy (policy) clearly whether the bank is going to adopt stable dividend policy, constant payout ratio or low regular plus extra dividends. The clearly defined policy will guide the way on how to follow dividend distribution. The bank should follow them (defined dividend strategy) strictly in normal condition. If there is lack of clearly defined dividend strategy, so many problems or inconveniences will be created to many other organizational sectors especially on the financial sectors.
- ❖ There is no clear-cut legal provision regarding dividend payments. So the government should act in favour of investors and should bind through such legal provisions or distinct rules so that the profit earning companies should distribute certain percent of their earnings as dividend.
- ❖ Banks should provide a chance to their shareholders for their interest. They should try to know whether they (shareholders) prefer to obtain cash dividend or stock dividend or any forms of dividend. So, instead of declaring cash or stock or any forms of dividend, dividend declaration should be proposed to the annual general meeting of shareholders for their approval. Furthermore, the banks should also be careful about informing the impacts of dividends, the advantages and disadvantages of different forms of dividend to those shareholders or potential investors who know less about the matters.
- ❖ The payment of dividend is highly fluctuating, which is neither static nor constantly growing. Such inconsistency and irregularity in the dividend payment may create more confusion and miss-conception about that firm. Due to higher degree of risk and uncertainty, such fluctuations impact the firm's market price per share adversely. So these banks are advised to follow either static or constantly growing dividend payment policy. Similarly, according to the changing context and shareholders interest and expectation, the predetermined policies should be reviewed.

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