CHAPTER - I

INTRODUCTION

1.1 Background of the Study

A bonus share simply is the payment of additional stock-to-stock holders in addition to cash dividends. It represents nothing more than a recapitalization of the company; a stockholder's proportional ownership remains unchanged. An issue of bonus share represents a distribution of share in addition to the cash dividend (known as stock dividend in the U.S.A.) to the existing shareholders (Hasting, 1966:370) The Rosenberg Dictionary of Business and Management define a portion of the net earning of a corporation payable (in share of fractional shares of designated stock of a given corporation) to the stockholders of record of corporation.

Bonus share is synonymous to stock dividend. It is a share whose disbursement is free. It is paid out of company's reserves. It is a free share of stock given to current shareholders based upon the number of share that a shareholder owns. While the stock action increases the no: of shares owned, it does not increase the total value. It is due to the fact that since the total no: of shares increases, the ratio of no: of shares held to no: of shares outstanding remains constant. Bonus share is a share issued fully or partly paid to the existing shareholder in a company. Bonus shares are usually issued in a pro-rata basis e.g.: a one- in- three bonus means that for every three shares held, one bonus share will be issued free.

Bonus share can also be understood as a dividend paid as additional shares of stock rather than as cash. It simply involves a transfer of Retained Earnings to the capital stock account. If dividends paid are in the form of cash, those dividends are taxable when a company issues a bonus share, rather than cash; they usually are not tax consequences until the shares are sold. Thus, bonus share are dividends paid in securities rather than cash. The dividend may be additional share issuing company, or in shares of another company usually a subsidiary held by a company.

After issue of bonus share the shareholders proportional ownership remains unchanged. But it affects the book value per share, the earning per shares, and the market per share because of increase in number of shares as a result of bonus shares.

It is an inexpensive way to raise the additional capital for growth and expansion. That is why bonus share issue has become an important and prevalent practice to increase the equity base internally.

Issuance of bonus share from the economic point of view has some differences from the accounting point of view. In the equity portion of the firm a bonus issue reduces the retained earnings and correspondingly increases paid up equity and share premium if any stock share split has no such effect. Issue of bonus share effects of bringing the market price of share within more popular range as a result of larger no: of shares outstanding. The larger no: of outstanding shares will also promote more active trading in the shares due to availability of floating stock. Yet another advantage might relate to the informational content the bonus announcement, the announcement is perceived favorable news by the investors in that with growing earnings. They look for increased future dividends. Moreover, it enables the effort to conserve cash for profitable investment opportunities, the share price will tend to rise and shareholder gets benefit. However, if the move to conserve cash relates to financial difficulties within the firm the market price will improve the prospect of raising additional fund particularly through the issue of convertible debentures.

In legal context, bonus share may have different meaning for the different groups of professional lawyers and practitioners. Company Act 2053 states the term bonus share as an additional shares issued to capitalize the company’s surplus and reserves. It also includes the capitalization of dividend in order to increase the paid up capital (Company Act 2053, Section 1, Clause 2, Sub clause ‘Da’). The bonus share can be issued only out of profits and reserves created f or profits, and prohibit issuing bonus shares from increasing share capital by revaluation of company’s assets (Section 4, Clause 42, Sub clause 5). The procedural requirement of declaring bonus share by the company is stated in section 5 clause 68. The Board requires bringing a special resolution for consent and approval by majority of its shareholders present in Annual General Meeting of the company. The accounting treatment of a stock dividend is to increase the ‘common stock’ and ‘paid in capital ‘accounts by an amount equal to the market value of the stock at the time of the dividend announcement times the number of new shares issued. In order to keep the total book value of stockholders’ equity the same, the retained account is reduced by an equivalent amount.

In a capital market, all firms operate in order to generate profit. Equity Capital is provided by the shareholders, so shareholders are also shared profits directly or indirectly. When a firm pays a portion of its profit to the shareholders, they are directly benefited. If instead of paying dividends, the firm retains the fund to explore other growth opportunities, the shareholders expects cash dividend.

Bonus Share may serve to keep the market price per share in a popular trading range appear to have an informational or signalling effect; when other things are held constant, share price tend to rise around the time of announcement consistent with positive signal. An integral part of dividend policy of a firm is the bonus share it involves the issuing new share on a pro-rata basis to the current shareholders while the firms assess its earning, the risk being assumed and the investor percentage ownership in the company remains unchanged.

In Bonus Share, the retained earning must be reduced by the rupee amount of Bonus Share. As Bonus Share are limited by the size of retained earning , only those corporate firms willingly announce the Bonus Share maintaining the minimum required level of retained earning. Since Bonus Share is perceived as a positive signals of improved performance & increase profitable investment. It’s natural that existing and prospective shareholders expect return to increase in the value of stocks.

The first Nepalese capital market was established as Security Marketing Centre in 1976 during seventh national plan in government sector. After establishment of new capital market development in 1992, helped a lot to establish the stock exchange market and trading floor for secondary market operation. The Government, Nepal Rastra Bank & Nepal Industrial Development Corporation owns it.

Corporate firms in Nepal have been practicing the bonus share (or stock dividends) as a means rewarding to the shareholders. Issue of bonus share is recent practice of Nepalese corporate firms despite of Nepalese capital market have crossed more than three decades. In our country, issue of bonus share took momentum only after liberalized economic policy to (Commercial) joint venture banks, which enhanced the bonus share issue in considerable number. Bonus share as a significant subject as it carries certain advantages both to shareholders and the company. Despite this very limited studies have been conducted so far. So it is felt necessary to study the impact of bonus share issue on market price the inputs to financial literature relating to the topic. This study could be a milestone and may provide additional information regarding bonus share issue.

1.2 Statement of the Problem

Bonus Share issue is a recent phenomenon of corporate firms in Nepal. Bonus Share is not a cash dividend. Bonus Share cannot be paid as cash dividend. As mentioned earlier, bonus share issue took momentum after the announcement of economic liberalization policy by government in mid-eighties such practice ignores the impact of bonus share on Earning per Share (EPS), Dividend per Share (DPS), and Market Price of Share (MPS). It may finally affect the small shareholders and the value maximization objective seems never to be achieved.

Theoretically, the issue of bonus share does not affect the wealth of shareholders. The earning per share and market price per share will fall proportionately to the bonus issue. For example, as a result of the increasing the number of share by 10%, the earning per share and market price per share should also fall by 10% all other things remaining equal. This theory may not be applicable in practice of Nepalese capital market, as the bonus share is not based on systematic mechanism and due to non-financial factors, the stock price in market does not match to the intrinsic value. In efficient market stock price used to be equal to the intrinsic value since the buyer and seller are fully informed about the financial factors. Bonus share issue practice is on ad-hoc basis. The reason behind this is not having an efficient market. Nepalese capital market is inefficient; investors are unaware of how to interpret the information and cannot make a rational decision regarding the transaction f bonus share. Thus, the stock price in Nepal is determined by other factors rather than the financial performance of the concerned company. Wrong information is provided to the general investors as a result leads to take wrong decision.

The problem of bonus share issue and impact on of market price per share of its share is not favourable. It has posed problem to the investors in portfolio planning and to economists to understand and appraise the functioning of the capital market in Nepal.

The numbers of shareholders in corporate sector have exceeded 300,000 in numbers in Nepal. Other than regular cash dividend, they have diverse interest reserve requirement to fulfil. Thus, another problem concerns with the legal consideration, which corporate firms should have to adhere to decrease dividends and bonus share.

The problem of bonus share issue is most of the shareholders think that they receive extra share of same value as existing value but the theory says the market value or shareholder's wealth does not change. For instance, suppose a company declares 1:2 bonus shares to its existing shareholders. The existing shareholders receive one additional share for two existing shares. The company provides bonus share mere transferring the amount out of reserve and retained earnings to paid-up capital. It does not affect company's assets and the total shareholders' equity of the company remains the same. Therefore it is just reshuffle of book of account.

Shareholders are not satisfied with the dividend policy of bonus share issue and practice. Management's attitude towards them and in maximizing shareholders wealth, while corporate executives are of different opinion on these issues so this study deals with the problem of analyzing and studying the differences of opinion reading bonus share issue and practice of corporate firms and how bonus shares affects the market price per share. This study deals with the following questions:

- What is the impact of bonus share issue on market price of share?
- Whether the bonus share issues positively affect the share price and do investor perceive bonus share positively?
- What are the characteristics features of bonus share issue practices of corporate firms?
- Is there any correlation between bonus ratio and share price increment?
- Do the Companies increase their quantum on share price after bonus share announcement?

1.3 Objective of the Study

The basic objective of this study is to understand and analyze the bonus share issue practices in Nepalese listed corporate and to evaluate the relation of bonus share announcement and stock price. The main objectives of the study are:

- To analyse and evaluate the existing situation of practice of bonus share issue of corporate firms in Nepal.
- To evaluate the practice of issue of bonus share and its impact in the market.

- To analyse the effect of bonus share in stock market.
- To provide suggestion and recommendation on the basis of major finding.

1.4 Significance of the Study

In view of the significant rate of dividend policy about bonus share, the corporate firms should follow the appropriate dividend policy about bonus share. Its practice has an important role in maximizing the shareholders value of investment. Bonus share issue is one of the important and critical variables affecting the market price of share. It affects the choice of the investments portfolio by the prospective investors. It is a significant subject as it carries certain advantages both to shareholders and the company. Despite this very limited studies have been conducted so for. So it is felt necessary to study the impact of bonus share issue on market price of share. This study is expected to fill the research gap and add to the inputs financial literature on bonus share issue and its impact on market price in Nepalese capital market, especially to the general investors, management and policy makers. The Nepalese corporate firms intend to announce bonus share, affect EPS, DPS and finally MPS, it is very important of decision of financial manager in financial management. The prevailing misconception about bonus share if any will be tried to remove. So this study of bonus share has considerable importance to investors, corporate management and economists.

1.5 Limitation of the Studies

The limitation of the study is as follows;

- This study covers the analysis of data during the period by 2003/2004 to 2007/2008.
- This study is only concentrated on issuance practice of bonus share of Nepalese listed corporate firms.
- This study is based on the secondary as well as primary data of the selected listed sample corporate firms, which have the bonus share track records.
- This study just analyzes the bonus share issue not entire dividend payment of corporate. It only observes the impact of bonus share on share price but does not isolate the impact of cash dividend at the same time when a particular company distributes cash dividend along with bonus share announcement.
- This study is for the partial fulfilment of MBS, so time constraint exists.

1.6 Organization of the Study

Organization of the study consists of the following;

I. Introduction: This chapter includes the introductory portion about Bonus Share issuance and its effect on market price of share. It contains introduction, statement of problem, objectives of the study, limitation of the study and the organization of the study.

II. Literature Review: This chapter includes the brief review of books, journals and previous researches. It includes discussion on the conceptual framework & review of major studies as well.

III. Research Methodology: This chapter includes research design, population and sample, nature and source of data and data processing procedure. It deals with the selected firms the model of analysis meaning & definition of statistical tools used.

IV. Data presentation and analysis: This chapter includes analysis and presentation of the collected data is known as Analytical framework. This is the main body of the study.

V. Summary, conclusion and recommendations: This is last portion of the study, which includes major findings, conclusions and recommendations. This chapter presents the major findings and compares them with theory and other empirical evidence to possible extend.

CHAPTER - II

REVIEW OF LITERATURE

2.1 Conceptual Framework

Announcement of bonus share (stock dividend) by the management is one of the crucial decisions. Bonus Share should not be on ad-hoc basis because it adversely affects the earning per share, dividend per share & market price per share. Before determining the issue of bonus share, firm must study its impact on earning per share and stock price.

Commenting on the work of Linter (1956), numerous studies have examined the Bonus share announcement policies of firms. Bonus share or stock dividend decision however is still a crucial as well as controversial area of “Managerial Finance”. The effect of stock dividend policy on a firm’s market value is a subject of long standing controversy. (Baker Edelman& Farrelly, 1985:78). Black epitomizes the lack of consensus by stating, “The harder we look at the dividend picture the more it seems like puzzle with pieces, with pieces, and just don’t fit together” (Black, 1976:5). So, bonus share announcement of corporate firms are not clearly understood by a large portion of the financial community.

Issuance of bonus share has always been a controversial topic, whether it maximizes the future market value or not. There are different schools of thoughts about the issue. One school of thought opines, A stock dividend simply is the payment of additional stock to stockholders. It means nothing more than a recapitalization of the company; a stockholders proportional ownership remains unchanged. (Van Horne, 1998:319). And another school of thought opines that if bonus share are accompanied by increase in earnings & cash dividend (quantum of dividend) causes the price, of the stock to increase immediately after bonus issue, and also due to issuance of stock dividend or stock split a reduction in the minimum trading range greatly increases a firm’s base of individual investors & its stock liquidity, is associated with a significant increase in stock price. (Yakov Amihud Haim Mendelson & Jun Uno, 1991:1169). Various empirical studies have been done on bonus share and stock prices in developed capital market. Few of them are Linter (1956), Modigliani & Miller (1961), Gordon (1962), Walter (1966), Van Horne & Mc. Donald (1971). However, no simple and conclusive relationship exists between stock dividend & common stock prices.

Even if bonus share do affect the firm's value, unless management know exactly how they affect value. There is not much that they can do to increase the shareholders wealth. (Solomon, 1973:142). Bonus share issue & practices thus provides an empirical question for this study. Among various empirical contradictions to Assets Pricing Model of Sharpe (1964), Linton (1965), Black (1972), the most prominent is the size effect of BANZ (1981). He finds the average returns on small stocks are higher.

Stock price in market is dominant by the non-financial sectors. So, it doesn't match with the intrinsic value. Thus, the theories depicted are not applicable in Nepalese context. In efficient market stock price used to be equal with the intrinsic value since the buyer & seller are fully ignored about the financial factors. Investors in Nepalese capital market do not know to interpret the information and therefore they cannot conclude rational decision regarding transaction of the share. In this context, stock price in Nepal is determined by other factors rather than the financial performance of the concerned firm. General investors are supplied with wrong information that leads them to take wrong decision.

The behavior of Nepalese investors is quite optimistic towards bonus share, whatever the cause behind the bonus share. Thus, where do these types of behavior of investors lead the capital market of Nepal? It is generally believed that declaration of issuing bonus share affects the market price of stock of the corporate firm. Corporate firms in Nepal are found following the practice of issuing bonus share time & again, Issuing bonus share is part of dividend policy & is common in practice.

Management may decide to announce cash dividend and issue of Bonus Share on the same date cash dividend involves actual paying of cash while bonus share simply involve transfer of retained earnings to the capital stock account. Issue of bonus share represents a distribution of share in proportion in addition to cash dividend to the existing shareholders.

Firms issues shares in lieu of consideration. The consideration may be either in the form of cash or stock. Stock dividend (Bonus Share) is issued to the existing shareholders without payment of any consideration either in cash or stock. Bonus share are issued by conversion of the reserves & surplus of the firms into shares. Apparently, Bonus share can be issued only by those firms which have accumulated large free reserves i.e.

reserves not set apart for any specific purpose and which can be distributed as dividend. However, bonus share can be issued out of balance in the share premium account. Issuance of bonus share simply splits the 'ownership pie' in to more pieces but does not affect the size of the pie. General belief is that the stock holders are worse off as a result of the payment of bonus share since issuing the new shares creates no value and the firm has to pay for printing and issuing of new shares. Technically, issue of bonus share is nothing more than an accounting transfer from retained earnings to the capital stock account.

As per the study of (Shrestha & Manandhar, 1992:35), it is concluded that the Nepalese corporate firms practices the bonus shares as a means of rewarding the shareholders. In 1992/93 Nepal Arab Bank Ltd, in its 5th annual meeting declared in principle 60% cash dividend, of which 20% was actual cash dividend and 40% cash dividend which was capitalized from profits which corresponds to Rs.12 million transferred from P/L account to equity capital resulting no effect in financial position. Then bank increased its equity capital from time to time by issuing bonus shares likewise, Nepal Bank ltd, Nepal Insurance Company, Himalayan Bank ltd & Bishal Bazar company ltd have also been found increased in equity capital many times by ways of issuing bonus shares.

Advantages of Issuing Bonus Share

- It bridges the gap between capital & fixed assets.
- Increases the market price of its shares
- Creates confidence for the investors/shareholders in company
- Good market reputation
- Increases liquidity of shares
- Increase the paid up capital of the corporate firms.

Disadvantages of Issuing Bonus share

- Issuance of shares does not realizes cash from shareholders
- Earning per share is reduced.
- Converts retained earnings into paid up capital
- Issuance of Bonus share leads to reduction in retained earning.

Reasons for Issuing Bonus Share

– **To Conserve Cash:**

Issue of bonus share does not involve the payment of cash like cash dividend. The bonus share allows the firm to declare dividend without using cash, which is needed for operation or expansion. Rather than seeking additional external financing the firm can retain its funds that would otherwise be distributed to shareholders. This process is known as capitalization of profit

– **To Indicate higher future profits:**

Generally, a bonus hare is an indication of higher future profits, bonus share usually is declared by Board of Directors who expect rise in earnings to offset the additional shares. Board of Directors does not wish dilution of earnings therefore must invest on profitable opportunities.

– **To bring the market price of shares within more popular range:**

Effect of bonus share is increase in the number of outstanding shares and decrease in share price after distribution of bonus shares. A share has a strong operating performance that leads to an increase in market value in popular range. Then the management of the firm determines that the price of the share is higher than (moving & of) the popular trading range & decides a bonus share would be useful to bring the higher priced share within the popular range where small investors are also able to trade and can include in their portfolios a large number of different stocks.

– **To increase the number of outstanding shares**:

Issue of bonus share increases the number of outstanding shares that promotes the active trading in the stock market. Since, small investors may be unable to trade the minimum unit as this requires a large amount of money, so a reduction in share price & holding additional number of shares enables them to trade & to diversify their portfolios.

– **To have positive psychological value**:

Announcement of bonus share is perceived as favourable news by the investors because of growing earnings, the company has bright prospects & the investors can reasonably took for increase in future dividends. As the investors take bonus share is an effort to reserve cash for profitable investment opportunities, the share prices have positive psychological value after a bonus share, and the price may actually rise.

– **To retain proportional ownership for shareholders:**

This is another alternative to meet company's additional equity capital by issuing new equity in capital market. If the existing shareholders do not have funds to purchase a new equity, their proportion of the ownership in the firm will decline as new investors purchase shares. This can be avoided by issuing bonus share, which is called recapitalization of profit. Each shareholder receives a number of additional shares proportionate to his original holdings. If a shareholder does not want to loose his proportional ownership in the company, he may not sell his share.

– **Tax benefit to the shareholders**:

When a shareholder receives cash dividend from Company, it includes in his ordinary income and taxed at the rate of ordinary income tax rate. But the receipt of bonus share by the shareholders is not taxable as income. If the shareholders want to sell the new shares received by the way of the bonus issue to satisfy his desire for income and pay Capital gain taxes, which are usually less than ordinary tax rate. The shareholders do not mind to sale the shares received by the way of bonus shares as they consider it a windfall gain and not a part of principal investment.

– **To achieve a more respectable size in the market:**

After bonus share issued by a firm every shareholder receives an additional share proportionate to original holding. Some of the old shareholders may sell their new Shares. As a result a corporate firm may achieve a more respectable size in the capital market.

– **To fulfil the legal requirement imposed by the authority:**

In the context of Nepal, Nepal Rastra Bank impose legal requirement for increasing the equity base at certain standard level. Therefore, the Bonus Share issue enthusiastically increases from 1992/93 by Corporate Firms listed in Nepal Stock Exchange. To fulfil their legal requirement, Nepalese Corporate Firms practices of raising the additional Capital from internal source because of the lower cost of funds, to save the floatation cost and to avoid the difficulties in raising external equity (Shrestha and Manandhar, 1998: 48).

– **To avoid external inconvenient:**

Investment financed from external sources is subject to screening by outside agencies as to its related profitability but investment financed from internally generated fund is subject to no such check.

2.1.1 Limitations of Bonus Share:

Previously, we discussed the main advantages of bonus share issue as a favourable psychological value on shareholders. It indicates the company's growth to shareholders. Thus, shareholders prefer bonus share though it has some limitations. Without proper study of profit planning issuance of bonus share might invite over capitalization. Some of the limitations of bonus share are as follows:

- Declaration of bonus share is a method of capitalizing the past earnings of the shareholders that they already own. So, it simply divides the ownership of the firm into a large number of share certificates. Hence, bonus share just represents a division of corporate pie into a large number of pieces.
- Issue of bonus share leads to an increase in the capitalization of the firm. It can only be justified if there is a proportionate increase in the earning capacity of the company. Otherwise, shareholders fail to realize that the bonus share do not affect their wealth.
- Some shareholders prefer cash dividends instead of bonus share; such shareholders may be disappointed as bonus share benefits them indirectly.
- Issuance of bonus share lowers the market value of existing share too. That may poses negative impact of particular share on capital market.
- The main disadvantages from the corporate firm's point of view are that they are more costly to administer than cash dividend. It can't be administered easily like cash dividend.
- Issue of bonus share results increased liability on the corporate firm in respect of future dividend. So bonus share issue can be disadvantageous if firm declares periodic small bonus shares.
- It deprives new investors from becoming the shareholders of the firm. The control over management of the firm is not diluted & existing management may misuse its position.
- Frequent announcement of bonus share may disfigure the price earnings to downwards.

2.1.2 Procedural and Legal Aspects

Firm must follow certain rules & regulation as mentioned in Company Act and their respective memorandum & Articles of Associations. In case of India, the controller of capital issues of India must approve issuance of bonus share. In Nepalese context under Company Act, 2053 Section 5 Clause 68 states the procedural requirement of declaring bonus share by the firm. The issuance of bonus share to the existing shareholders is governed by the Company Act 1997 (2053 B.S), and in case of commercial banks by the Commercial Bank Act, 1974 (2031 B.S), & subsequent amendments thereon in addition. Company Act, 1997 Section 21 Clause'd' required the corporate firm to state the point relating to the bonus share issue in the prospectus. Section 42, Sub Section 3 of the Act stated that in case of need of issuing bonus share corporate firm is not required publishing the prospectus. Sub Section 4 of the same section is concerned with the issue of bonus share to the corporate employees. The Sub Section restricted the issue of bonus share if management thinks necessary to appropriate not more than 5% of the increased capital to the employees of the corporation.

- Section 68 requires the corporate management to table the passed special resolution regarding the issue of bonus share in the Annual General Meeting.
- Corporate management should inform to the concerned authority (SEBON) before issue of bonus share. (Company Act, 1997 Section 137)
- Section 42, Sub Section 5 disqualifies the corporate firm in increasing share capital or issuing bonus shares from reserves & surplus created by revaluation of corporate firms' assets except earned profits.

Regarding share capital & distribution of dividend, Commercial Bank Act 1974 and subsequent amendments there on also govern commercial banks. Section 14, Sub Section 5 stated that commercial banks have to increase their authorized, issued & paid up capital as per directives given by NRB (4^{th} amendment, 1989) Section 18 restricted the commercial bank to announce the dividend unless it has recovered the preliminary expenses, debit balances of profit & loss account & build capital reserve, risk bearing reserve and general reserve as required by policy provisions (4^{th} amendment 1989). The government budget speeches & policy directives by NRB changed these provisions later on from time to time.

These new provisions relating to the paid up capital of commercial banks have directly affected the dividend policy & practices of old commercial banks. Most of the commercial banks are bound to review & change their dividend practices in terms of dividend rate & amount. Even if they have capacity to pay higher rate of dividend, commercial banks are indulge to maintain higher reserves & surplus by retaining more earnings so that corporate management can attain minimum level of paid up capital as directed by NRB.

The important events & dates in the bonus share payment procedure are as follows:

– **Board Resolution:**

Under Company Act 053, a public company should have formal meeting of Board of Directors at least six times within a financial year. The bonus share decision is the right of the Board of Directors. Therefore the board of directors brings a special resolution for bonus issue. The Board of Directors of the company should make application for issue of bonus share within one month of the bonus announcement. (Khan & Jain, 1992: 600)

– **Shareholders' Approval:**

The resolution of the Board of Directors to distribute the bonus share has to be approved by the shareholders in Annual General Meeting. A chance of disapproving the resolution of Board of Directors is very low. But in context of Nepal, a case can be found that a corporate firm did not distribute bonus share to the shareholders even after its declaration.

– **Record Date:**

The bonus share is payable to shareholders whose names appear in the Registers of Members as on the record date. If a shareholder sells shares before record date, the buyer of shares will receive bonus shares. If a shareholder sells shares after record date, the seller of the shares will receive bonus share as his/her name is recorded in the register of members instead of buyer.

– **Bonus Share Payment:**

Once a bonus share declaration, has been made along with book close date for share transaction, corporate firm has to distribute bonus share within certain period to the shareholders. But due to lack of information the investors are provided bonus share even one year after bonus share issue. As we know that Nepalese capital market is in infancy period, the lack of awareness of the investors and inadequate practice and expertise may be the consequences of the situations.

2.1.3 Conditions for The Issue of Bonus Share

In case of Indian corporate firms, they must be approved from controller of capital issues of bonus share. Though there is not such type of approval required for the Nepalese corporate firms. Still, a corporate firm should maintain following condition for the issue of bonus share.

- A corporate firm is not allowed to declare bonus shares except if not partly paid up shares have been converted into fully paid-up shares. But the firm can capitalize the company's surplus and reserves in order to increase the paid-up capital as dividend capitalization.
- Bonus share can be issued out of profits and a reserve created from profits but prohibits issuing bonus share from increasing share capital by revaluation of firm's assets.
- A corporate firm can declare bonus share once a year. The firm may make a further application for issue of bonus shares only after 12 month, from the date of sanction by the government of an earlier bonus issue, if any.(Khan & Jain, 1992:599)
- A resolution approving the proposal of the bonus issue, the firm's shareholders on the occasion of annual general meeting should pass clearly indicating the rate of dividend payable on the increased capital.
- Regarding American cases, stock dividend cannot be issued through past-accumulated reserves and surplus. They can only issue stock dividend out of current reserves & surplus. Stock dividend cannot be issued out of previous accumulated reserve and surplus because these might be pledged for the loans of the firm.
- Total amount to be capitalized by issue of bonus share out of reserves shall not exceed the total amount of paid-up equity capital of the firm.

2.1.4 Theoretical Value of Bonus Share & Accounting Treatment

The investors receive ownership of additional shares of common stock without injecting additional funds. Their proportionate ownership on the company is unchanged. This may be a reason for issue of bonus share to the existing shareholders on pro-rata basis.

A firm declares appropriate bonus ratio as per its objectives & convenience of the management. If a firm declares 3:1 bonus share, it means investor having three original common stocks receives one additional share. In another way, one extra share for original three shares.

Theoretically, the market pr ice of the stock should decline proportionately to the bonus ratio. Therefore, the total value of each shareholders holding remains same. But in practice it is contradict to the doctrine under imperfect capital market.

The consequences of a bonus issue:

- The stockholders' proportional ownership remains unchanged.
- The book value per share, the earning per share and the market price per share decrease.
- The number of outstanding share increases.

From the accounting point of view, issue of bonus share is a reshuffle of the capitalization in the equity portion of the balance sheet. When stock dividend is paid, a portion of the surplus (retained earnings) is transferred to the capital account & shareholders are issued additional share certificates. Bonus share is provided through retained earnings. A bonus share reduces the retained earnings and correspondingly increases paid up equity & share premium (if any).

Table (A) elaborates the effect of bonus share on the capitalization of the firm. The table shows the equity portion of the balance sheet before and after the bonus issue.

TABLE 2.1 (A)

The Effect of Bonus Shares

(I) Equity portion before the bonus issue:

Equity share capital (20000 shares @ Rs.100)	Rs.2000000
Share Premium @ Rs.75	1000000
Retained Earnings	8000000
Total Equity	11000000

(II) Equity portion after bonus issue (2:1 bonus ratio)

Equity share capital (30000 shares @Rs.100)	3000000
Share Premium @Rs.50	1500000
Retained Earnings	6500000
Total Equity	11000000

Source: Corporate Finance: Principles and problems (Kuchhal,S.C)

: Principles of Managerial finance (Lawrence.J. Gitman)

Table 2.1 (B) illustrates how a share of stock originally selling for Rs.100/ per share can fall to Rs.50/ per share on 1:1 (100%) bonus share issue without changing the owner's 5% rate of return. The hypothetical change in the unit of account occurred between period 2 & 3. The existing shareholders own twice as many shares after the bonus share issue. But since each share has half the previous market price, the market value of the investor's total investment is unchanged. The investor's income is Rs.5 of cash dividend per period per Rs.100/ of investment.

TABLE 2.1 (B)

Bonus Share Issue

	Period 1	Period 2	Period 3	Period 4
Market price per share (Rs)	100	100		
Cash dividend per share (Rs.)	5	5	2.5	2.5
Earning per share	10	10	5	5
Number of shares held per Rs.100 original investment	1	1	2	2
One period rate of return	5%	5%	5%	5%

Source: Corporate Finance: Principles and problems (Kuchhal,S.C)

: Principles of Managerial finance (Lawrence.J. Gitman)

Van Horne & Wachowicz (2000:10:4948) suggest that accounting authorities should make a distinction between small-percentage stock dividends and large percentage stock dividends. The effect of stock dividend on common stock will be different magnitude on different ratio of stock dividend. The impact of small percentage stock dividend on share price is less than the large-percentage stock dividend. Therefore, they recommend different accounting treatment for them.

(A) Small-Percentage Stock Dividend:

If a stock dividend represents an increase of less than 20% of the previously outstanding common stock, it is referred as a small-percentage stock dividend. Accounting for this type of stock dividend entails transferring an amount from retained earnings to common stock and additional paid in capital (share premium).(Van Horne,2004:325)

It can be explained by a hypothetical example. If a corporate firm has a total shareholders' equity (before issuing a stock dividend) as shown on the left-hand side of the table 2(A). The fair market value of the stock is 40 per share. The firm issues a 5% (1:20) stock dividend, amounting to 20000 additional shares (400000 x 0.05) of stock. For each 20 shares gets one additional share.

TABLE 2.2(A)

5% (1:20) Stock Dividend

BEFORE		AFTER	
Common stock (400000 shares @Rs.5 Par)	2000000	Common Stock (420000 shares @Rs.5 par)	2100000
Additional paid-in capital	1000000	Additional paid –in capital	1700000
Retained Earning	7000000	Retained Earning	6200000
Total Shareholders Equity	10000000	Total shareholders equity	10000000

Source: Corporate Finance: Principles and problems (Kuchhal,S.C)

: Principles of Managerial finance (Lawrence.J. Gitman)

The amount of the stock dividend is calculated on market value of the stock i.e.Rs.800000 (Rs.40/ X 20000 Shares). The amount of the stock dividend is transferred from retained earning to the common stock & remaining to the paid in capital. Par value of the shares must be same as it is. Thus, the amount, carried from retained earning, transferred to the common stock only by 100000 (5 par X 20000 additional shares) is entered into reshuffle of equity capital therefore the total shareholders equity of the firm remains same.

Does the Earning per Share changes after distribution of stock dividend? Earning per Share of the company is reduced proportionately as increment of common stock by 5%. Suppose if the same corporate firm's earning is 1,000,000/- after tax.

	Before stock dividend	After stock dividend
Earning after Tax (Rs)	1,000,000/-	1,000,000/-
No. of Outstanding Shares	400,000/-	420,000/-
Earning per Share (EPS)	2.50	2.38

Source: Corporate Finance: Principles and problems (Kuchhal,S.C)

: Principles of Managerial finance (Lawrence.J. Gitman)

Shareholder's have more shares of stock after stock dividend but have lower earning per share (EPS). In reality every shareholder's proportionate ownership claim against total earnings available to common shareholders' (no: of share holding X EPS) remains unchanged.

(B) Large –Percentage Stock Dividend:

If a stock dividend presents an increase of more than 20% of the previously outstanding common stock, it is considered as a large percentage stock dividend. This type of stock dividend should be treated differently for accounting purpose. Small-percentage of stock dividends is not expected to have much effect on the market value per share to stock. But large-percentage of stock dividends is expected to materially reduce the market price per share of stock. Therefore, in such cases, conservation argues for reclassifying an amount limited to the par value of additional shares rather than an amount related to the pre-stock dividend market value of the stock.

TABLE 2.2(B)

100% (1:1) Stock Dividend

BEFORE		AFTER	
Common stock (400000 shares @Rs.5 Par)	2000000	Common Stock (800000 shares @Rs.5 par)	4000000
Additional paid-in capital	1000000	Additional paid –in capital	1000000
Retained Earning	7000000	Retained Earning	5000000
Total Shareholders Equity	10000000	Total shareholders equity	10000000

Source: Corporate Finance: Principles and problems (Kuchhal,S.C)

: Principles of Managerial finance (Lawrence.J. Gitman)

If the same corporate firms mentioned above, decided to issue a 100% (1:1) stock dividend instead of 5% stock dividend. The consequence of the stock dividend on shareholders equity section of the firm's balance sheet is presented in Table 2-B.

The stock dividend amount is calculated on par value of common stock. Because of the 100% stock dividend, the addition 400000 shares are transferred from retained earnings to the common stock (at par value) account. The total transferred amount is 2000000 (5 X 400000).

2.1.5 Criteria for Bonus Issue

Stock dividends are issued in addition and not in lieu of cash dividend in India. A firm is not allowed to declare bonus share unless partly paid-up share have been converted into fully paid-up shares. Stock dividends are made out of share premium and free reserve, which includes investment, allowance reserve but excludes capital reserve on account of assets revaluation. In short time the amount of stock dividend issue should exceed the paid-up capital. A firm can declare stock dividend once in a year. A resolution approving he proposal of the stock dividend issue clearly indicating the rate of dividend payable on the increased capital should be passed by the firm's shareholders. Firm intending to issue stock dividend should not be in default of payments of statutory dues to employees and term loans to financial institutions.

Generally, the maximum bonus share ratio is 1:1 i.e. one share for one fully paid-up share held by the existing shareholders. However, two criteria must be satisfied within the limit of the maximum ratio.

1. <u>Residual reserve criterion</u>

In this criteria, reserve remaining after the amount capitalized for bonus share issue should at least be equal to 40% of the increased paid-up capital. But redemption reserve and capital reserve on account of assets revaluation are excluded while investment allowance reserves are included in computing the minimum residual reserve. This criterion is illustrated as follow:

Pre-bonus reserve - (Pre-bonus paid up capital Bonus ratios) $\geq$ 0.4 (1+ bonus ratio) x Pre-bonus paid up capital

2. <u>Profitability Criterion</u>

In this criterion, 30% of the previous three years average pre-term profit (PBT) should be at least equal to 10% of the increased paid up capital. This criterion is illustrated as follow:

0.3 Three year Average PBT $\geq$ 0.1 (1 + Bonus ratio) x Pre-bonus paid up capital.

After compilation of both residual reserve criterion and profitability criterion, lesser bonus ratio will be allowed to declare bonus issue to the company.

2.1.6 Impact of Bonus Share Issue

If the corporate management felt the need and if they have to comply with policy directives given by concerned authority to increase the capital base from time to time a number of corporate firms announces and issues bonus share to increase their capital base. In the content of our country, NRB acts as the regulatory body & issues directives to the commercial bonus to control and supervise the establishment and operation of commercial bank in Nepal. NRB in the year 2006 has revised the directives regarding the requirement of increasing minimum paid up capital in commercial banks, which significantly affects the bonus issue practice of commercial banks in Nepal Corporate firms, other than in banking sector can issue the bonus share to their shareholders by the corporate management as per the rules & provisions in company Act 1997.

Some of the corporate firms issue Bonus Share to their existing shareholders in order to compensate the decrease in dividend yield. Dividend yield decreases because of rapid increase in the market price of the shares compared to increase in nominal rate of dividend. Cash dividend divided by paid-up price of share gives nominal rate of dividend. Due to rapid growth rate and partly under capitalization, the market price of stock of such firms increases rapidly. The value of existing shareholder’s stocks rises, as a result nominal dividend rate seems attractive, dividend yield decreases and continue to be lowered. Thus, to compensate the existing shareholders for their increased value of investment and also to rectify the effect of under capitalization, bonus shares are issued to them by the corporate management which help to raise up the dividend yield in future because of the effect of decrease in market price of share.

According to (Chandra,1994:540-541) the specific cause for the corporate firms to issue Bonus Share are as follows: -

- To bring the market price of the stock in most popular range.
- To increase the number of shares and to promote active trading in he stock market.
- To minimize the adverse effect of high nominal dividend rate and to minimize the effect of profiteering in the market.
- To increase the share capital base.

- To improve the prospects of raising additional fund
- To gain the confidence of stockholders in the prospects of the corporate firm and in increasing the total dividends.

2.1.7 Effect of Bonus Share Issue

In an efficient market, issue of Bonus Share causes decreases in market price per share in a proportion of bonus issue ratio, so, shareholder's wealth is not affected. However, if market is inefficient, corporate management decision to issue Bonus Share in any ratio as expected by the shareholder's might have psychological effects on existing shareholders that may have favorable impact in share price. Share price is expected to increase normally because shareholders interpret the issue of Bonus Share as indication of corporate firm's prospect of higher profitability and expectation of increase total cash dividends.

Issue of bonus share increases the number of outstanding share but does not change the shareholder's proportional ownership pattern. Shareholders retain the proportional ownership in the corporate firm & total net worth remains same. There is only adjustment of the paid up share capital. Bonus share issue has a definite advantage to the corporate firm also. Generally, bonus share may be accompanied by increased cash dividends, which have positive effect in shareholder's wealth in future period of time. Issue of bonus share does not make a cash drain from the bank balance of the corporate firm as payment of cash dividend does. It conserves cash, as it is a popular means to pay dividend under financial difficulties and at the same time helps to bring the market price of share in most popular range. Thus, in order to avoid the borrowing in case of cash shortage for payment of cash dividend, corporate firms issue bonus share. In cash dividend the total assets and net worth of the corporate firm is reduced. As such the market price of the share, in most of the cases in an efficient market, decreases by the amount of cash dividends distributed. It is believed that neither the firm nor its shareholder's benefited or loose after issuance of bonus share unless there is an increase in the dividend payout ratio or stock price earning ratio. Generally, shareholders expect increase in dividend payout ratio in the future years as a result of bonus share issue. In another words, increase in earning do not accompany bonus share issue, such issue does not benefit shareholders in term of value of stocks. There is though that shareholders get increased cash dividend because of increased dividend payout ratio, hence it seems increased cash dividend not because of bonus share.

Bonus share is expected to project and image of growth hopefully and create a favorable impression on existing & prospective shareholders and also more protection for shareholders in the event of financial difficulties by capitalizing the retained earnings into common stock and/or additional paid in capital; issue of bonus share may have favorable impact on market price of stock in subsequent years.

2.2 Bonus Share & Stock Split

Number of outstanding shares changes with bonus share and stock split. However both are different in degree/importance & in accounting treatment. After stock split all the old shares are destroyed and new ones are issued with a new par value. But after issue of bonus share existing shareholders receives an additional shares as per the bonus ratio. Hypothetically, if a shareholder owns 20 shares at the time when 1:10 bonus issue is made, he will receive 2 additional shares. Means 10 old shares get one additional new share.

Under accounting treatment, in case of bonus share, the balance of reserves & surplus account decreases due to a transfer to the equity capital and the share premium accounts. The transferred amount must be equal to the market value of the share at the time of bonus share issued. Thus, par value remains same with a share split; the balance of the equity accounts does not change but par value per share changes.

For identical treatment, the New York Exchange has adopted a rule calling all distributions of stock under 25% per share stock dividend, and distributions over 25% stock splits even if the corporation involved call its action something different(Francis,1998:54). A stock split is similar to a bonus issue from the economic point of view, though there are some differences from the accounting point of view. A comparison between a bonus issue and a stock split is given below:

Bonus Issue	Stock Split
– A part of reserves is capitalized	– There is no capitalization of reserves.
– The par value of the stock is unchanged.	– The par value of the stock is reduced.
– The stockholders proportional ownership remains unchanged.	– The stockholders proportional ownership remains unchanged.
– The book value per share, the earnings per share, and the market price per share decline.	– The book value per share, the EPS, & the market price per share decline.
– The MPPS is brought with a more popular trading range.	– The MPPS is brought within a more popular trading range.

2.2.1 Bonus Share vs. New Share Issue

The bonus share differs from an issue of new equity share. If a firm needs finance it can obtain fund by selling new shares. To sell new shares in market a firm must bear flotation costs. If a Company is concerned about maintaining control and flotation costs are high, it might be reluctant to sell new common Stock. Therefore, to save the flotation cost and to avoid difficulties in raising external equity, a corporate firm can raise additional capital from internal sources. A Company can use bonus share, as they are less expensive alternative source of Capital.

2.2.2 Bonus Share vs. Cash Dividend

The distribution of a stock dividend in various circumstances becomes an effective method of conveying the shareholders an assurance about the profitable reinvestment of the retained profits. The stock dividend represents a certificate indicating the amount of reinvestment made on behalf of each shareholder. (Baumol,1965:55). But there is no obligation on the management to ensure that the reinvestment of past accumulated profits& reserves (retained income) via issue of bonus share yields a reasonable return for shareholders, therefore, most investors express doubts about the retained earning being taken at their face value or being invested in sufficiently remunerative schemes. Sometimes, most corporate firm pays dividends in the form of cash. Cash dividends may be supplemented by a Bonus issue (Stock dividend). A firm should have enough cash in its bank account, when cash dividends are declared. If it does not have enough bank balance, borrowing should make arrangement. When the firm follows a stable dividend policy, it should prepare a cash budget for the coming period to indicate the necessary funds, which would be necessary to meet the regular dividend payments of the firm. It is relatively difficult to make cash planning in anticipation of dividend needs when an unstable policy is followed.

The cash account and reserves account of a firm will be reduced when the cash dividend is paid. This has the effect of increasing the number of outstanding Shares of the firm. Moreover, unless there is a special tax consideration Shareholders may be justifiably suspicious of companies, which retain an exceptionally high proportion of earnings and thus decline to submit to the financial scrutiny and discipline involved in raising external equity (Merret&Sykes,1966:46). Dividends are relatively unprofitable investments. The present result, therefore, seem to tend some weak support to the view that institutional or fiscal arrangement which limits dividends are relatively inefficient method of increasing investment (Bulletin of the Oxford institute, 1962:412)

There are some other controversial reasons between Bonus Share and Cash dividend:

– **Liquidity Position:**

A Company whose liquidity position is weak, they should not distribute cash dividend. To conserve outflow of cash it could issue bonus shares to shareholders and that may also prevent from dissatisfaction of Shareholders. Though, Bonus Share announcement, a firm can improve its liquidity crisis and also satisfy its shareholders.

– **Degree of accumulated retained earnings:**

A firm with abundance of accumulated retained earnings has higher Share price than the popular range. Having good opportunities and high tax investors a firm do not want to distribute cash dividend and also want to keep share price within the popular trading range, then it must issue bonus share. A higher share price leads its stock illiquidity, because that cannot facilitate trading in the stock by small investors. A security's value is decreasing in its illiquidity costs because investors require compensation for these costs.

Therefore, increasing the number of investors who can hold a security should be value increasing. An increase in the number of investors holding a security should increase the firm's value.

- **Legal requirement or desire to increase paid up Capital:**

If a corporate firm wants to increase its paid up capital to meet its legal requirement, it can adopt any alternatives among three alternatives decisions: Bonus share or stock dividend to the existing shareholders, Right share (Each stockholder is issued an option to buy a certain number of new shares, and the terms of options are included on a piece of paper) and issue of new shares. If the corporate firm has smooth liquidity position and earnings, it will be better to issue bonus share rather than other alternatives.

2.2.3 Repurchase of Share

The number of outstanding shares is increased through bonus share issue, but stock repurchase helps to reduce the outstanding shares. Share repurchase has inverse objective than the bonus share. Share repurchase is the buyback of the share by the issuing firm. Share repurchase have the effect of raising share prices so that shareholders can be taxed at the capital gain rate instead of ordinary dividend rate on cash dividend. Corporate firm can repurchase its shares through a fixed price self-tender offer, a Dutch auction, and an open market purchase.

Repurchasing of share is considered as a part of dividend policy. If a firm has excess cash & insufficient profitable investment opportunities to justify the use of these funds, it may be in the interest of the shareholders to distribute the funds. The firm has two alternatives to distribute the cash whether repurchase shares or increase cash dividend. These two alternatives should make no difference to shareholders, theoretically, in the absence of personal income taxes. With repurchase, fewer shares remain outstanding & earning per share (EPS) and ultimately, dividend per share (DPS) rise. As a result, the market price per share (MPS) rises as well.

Some reasons for stock repurchase:

- To have share available fort he acquisition of other companies.
- Wishing to 'go private' by purchasing all of the outstanding shares.
- Having full intention of retiring it.

- To serve as a tax advantageous substitute for dividend payout. In the case of share price rise, shareholder can be taxed at the capital gain instead of ordinary tax for cash dividend.
- For positive signaling effect at the share undervalued situation.
- To change its capital structure.

Re-purchase effect:

- Stockholders reduce the number of outstanding Shares.
- It increases EPS and DPS if the payout ratio is not changed
- It increases the proportional ownership of existing stockholders.
- It increases the stock purchase as net worth per share increases.

2.2.4 Forms of Dividend:

In general, cash dividend is known as the form of dividend. A firm, according to its policies, objectives and situation, distributes different kinds of dividend to its stockholders. The type of dividend that firms follow is partly of a matter of attitude of directors and partly a matter of the various circumstances and financial constraints that bound corporate firm's plans and policies. (Shrestha, 1980: 670).

Dividend refers to the distribution of earnings to the ordinary shareholders of the firm in return to their investment. Normally, an investor expects to have return on his /her investment in the forms of dividend and capital gain. After the successful completion of fiscal year having sufficient profits management decides to declare dividend to shareholders and retain the profit in the firm. Therefore, one of the major reasons for which an investor is interested to invest money on shares of different institutions is dividend.

As mentioned above a corporation provides different types of dividend to its shareholders on the return of their investment. On the concentration of firm's policies, objectives and circumstances the following types of dividends are provided:

CASH DIVIDEND:

According to the name cash dividend is distributed to the stockholders in the form of cash out of the firm's earnings. The stockholder gets cash dividend as a return on the investment on pro-rata basis. Cash dividend drains out cash from the corporate firm. Consequently, both Total Assets and Net Worth of the firm decreases. The market price of the share drops in most cases by the amount of the cash dividend distributed. (Hasting, 1966:370).

Most corporate firm pay dividend in cash. When cash dividend is declared the corporate firm should have enough cash in its bank account.

STOCK DIVIDEND (BONUS SHARE):

A corporate firm can distribute additional common stock to its existing shareholders; this is called stock dividend or Bonus Share. A Shareholder's proportional ownership in the firm remains unchanged after stock dividend. The market price of the stock should decline proportionately. Theoretically, it is frequently used to conserve cash and to reduce the cash dividend pay out ratio of the firm. (Van Horne & Wachowicz, 2001: 497).

PROPERTY DIVIDEND:

Property dividend involves a payment of assets/property in any form other than cash. Whenever, the assets, which are not used in the operation of the business or in extra ordinary circumstances, are distributed to the shareholders who are the actual owners of the firm. For example, a Company can distribute its own products or the securities of subsidiaries.

BOND DIVIDEND:

Corporate firm can distribute its own bond to the shareholders on the name of bond dividend. It helps the firm to postpone the payment of Cash. To avoid cash outflow firm follows such types of dividend.

SCRIP DIVIDEND:

If the firm's share has been successfully trading on the stock market for a long time, and the price has become very high, the firm may make a scrip issue. Scrip dividend is similar as bonus share issue. Under this method of dividend, firm issues transferable promissory notes that might be interest bearing or not to the shareholders. When earnings of the company justify dividends, but has shortage of cash and want to conserve cash, it may declare scrip dividend to satisfy its shareholders expectation.

In the context of Nepal, only cash dividend and stock dividend (Bonus Share) are in practice.

2.3 Review of Books and Journals

Linter Study (1956)

J. Linter conducted a study in 1956, **"Distribution of Income of Corporation among Dividends, Retained Earning and Taxes"** which is focused in the behavioural aspect of dividend policy. He investigated dividend pattern of 28 different companies of America and found that, firm generally predetermines the desired payout and tries to achieve it and rarely considers other factors. The model developed from his research is as follows:

$\mathbf{D_t = P, EPSt}$

$\mathbf{D_t = D_t - 1 = a + b\ (D_t - D_t - 1) + e}$

Where,

D_t = Desired dividend

EPS = Earning per share

P = Targeted payout ratio.

a = Constant relating to dividend growth

b = Adjustment factor relating to previous period's dividend and desired level of dividend and desired level of dividend (b>1).

Major findings of this study are as follows:

- Firms generally prefer desired proportion of earning to be paid as dividend.
- Investment opportunities are not considered for modifying the pattern of dividend behavior.
- Firm generally have target payout ratios in view while determining change in dividend per share.

L.C. Gupta's Study (1973)

Gupta (1973) conducted an empirical study on "**A Study of the Dividend and The Price Effects of Bonus Share Issued",** which has become a milestone for students of corporate finance, professional among the corporate management, the stock exchange community, the stock exchange academicians and the institutional and non-institutional investors. This study, attempts to test some popularly held beliefs about the effect of bonus share issue on dividends and share prices. It examines the practices among the

Indian companies regarding the making of bonus issues and explores the interest controversy whether, and to what extent, such bonus issues represent real gains to their recipients. In the light of the empirical results obtained. The study goes on to examine the taxation, regularity and managerial aspects of the problem. The study shows overall picture of prevailing practices among Indian companies with regard to bonus share issues and the dividend effect and the price-effect of bonus issues.

The period of study extends over twenty-four years from 1948 to 1971.The coverage is restricted only to Indian Companies quoted on any stock exchanges. The study covers a total of 919 (+225) bonus issues. The coverage of analysis can be taken as representing an almost complete census of bonus issue made by companies with a stock exchange quotation at the time of bonus issues, excepting some of the specific exclusions.

The basic objectives of the Study were:

To study the effect of bonus share issues on dividends and share price changes associated with bonus issue. Some of the important specific questions to which this study concentrates to analyze**:**

- To what extend can bonus issue announcement be regarded as indicating the management's intention of increasing the dividend distribution in the near future?
- An increase in the dividend quantum does follow a bonus issue?
- What is the magnitude of dividend increase and is this magnitude directly related to the ratio of bonus issue?
- Whatever the aggregate maker valuation of a Company's equity increases as a result of bonus issues? For this question the study examine the immediate, as also the long- term, effect of bonus issue of the market valuation of a company's equity after adjusting specifically for the general market movement in share prices.
- It specifically examines how far bonus shares represent a real addition to the shareholders' wealth and income.
- To investigate the characteristics features of bonus issues by the Indian Companies. The study makes available for the first time a factual analysis of the prevailing practices amid Indian Companies regarding the issue of bonus shares. The examination throws light on several aspects of corporate financial policies and practices regarding bonus issues, such as bonus ratios, the frequency and regularity

of such issues by individual companies, and the relation of bonus issue to the size and age of companies.

- The analysis is intended to remove some of the widely held misconceptions about bonus shares.
- To examine managerial decision-making relating to bonus issues. Does the widely held belief that management tries to maintain the existing dividend rate even after bonus issue have any validity?
- The implications of the findings for the Government's taxation and regulatory policies and managerial decision relating to bonus issue have also been examined.
- Gupta used simple statistical tools such as percentage, frequency distribution, average and standard deviation to study and analyze the data. The original report was subsequently revised and simplified to make it of wider interest, without altering the basic framework and the major conclusions. His study was wide coverage and immense on bonus share.

Following findings were observed in study with bonus share:

- The sudden burst of enthusiasm for bonus issues (which accounted for a little over a half of the total amount and slightly under 40% of total number of bonus issues for the entire period) in 1966-1967 was caused by the abolition of the special tax levied on bonus issues since 1959.
- The great majority of the bonus issues in India are in relatively high ratio of 20% (i.e, 1:5) and above.
- Indian Company of irregular interval without any consistent policy makes the bonus issues. Therefore, he suggest a policy of an annual 'stock dividend' paid concurrently with the retention of profits has distinct advantages over the present practice in India of capitalizing past accumulation at infrequent and irregular intervals according to the whims of the management.
- The increase on dividend distribution was not quite as universal as is commonly believed and almost one-third of the cases showed no increase in the quantum of dividend distribution following the bonus issue.
- He concludes that an increase in the quantum of dividend distribution was more universal in the case of lower bonus ratios than in the case of higher ratios. And also

was more universal among companies with lower nominal dividend rates than among those with higher rates before the bonus issue.

- His analysis shows that bonus issues are often, but not invariably, accompanied by intentions to raise the dividend payment in immediate future.
- The analysis discloses that relatively sharp jumps in dividend are for more common than gradual increases among Indian Companies.
- There is no systematic relation exists between the bonus ratios on the one hand and the percentage of dividend rates, and lower ratios more often among companies paying low dividend rates.
- Shareholders will gain from a bonus issue only to the extent the bonus issue is associated with an increase in the quantum of future dividends.
- The analysis shows that the market has anticipated the board's decision to issue bonus share by several week before the actual decision, which is reflected in the fact that a part of the price raise resulting from bonus decision had taken place a month before the board's decision. This rise may be accounted for by the activities of 'insiders'.
- The immediate impact of bonus announcements on the share price is almost invariable favorable, the reason being that a bonus announcement is usually interpreted as indicating the management's intention to increase the dividend distribution in immediate future. The actual magnitude of the price rise will depend on the expected dividend increase together with the degree of confidence with which such expectations are held in each case.
- In most cases, the public was provided with very little information about the real motives behind a bonus issue. Hardly on the future rate of dividend.
- The speculative price rise that occurred immediately after bonus announcement was frequently based not so much on a realistic appraisal of the fundamental factors governing profit and dividend as rumours and psychology.
- The analysis finds that the positive correlation between the magnitude of price rise and the bonus ratio, even in board terms, disappears by the end of one year after bonus announcement. The extent of price after one year shows no regular tendency.

Walter's Model:

Professor James E. Walter argues that the choice of dividend policies always affects the value of the enterprises. His model is one of the earlier theoretical works, which shows clearly the importance of the relationship between the firm's internal rate of return, r, and its cost of capital, k, in the determining the dividend policy that will maximize the wealth of shareholders. Walter's model is based on the following assumptions (Pandey, 1975:741)

- The firm finances all investments through retained earnings; that are debt or new equity is not issued.
- The firm's internal rate of return, r and its cost of capital, k, are constant.
- All earnings are either distributed as dividends or invested internally immediately.
- Beginning earning and dividends never change. The values of the earnings per share, EPS, and the dividend per share, DIV, may be changed in the model to constant forever in determining a given value.
- The firm has a vary long of infinite life.

Walter's formula to determine the market price per share is as follows:

$$\mathbf{P} = \frac{Div}{K} + \frac{r(EPS - DIV)}{K}$$

Where,

P= Market price Per Share

DIV= Dividend Per Share

EPS= Earning Per Share

r = internal rate of return (average)

k = cost of capital or capitalization rate

In 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's view of the optimum dividend- payout ratio can be summarized as follows:

Growth Firms, **r > k**:

Firm having **r > k** may be referred as growth firm. 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 Firms, r = k:

Firm having **r = k** may be referred as normal firm. There is no unique optimum pay out ratio for a normal firm. One dividend policy is as good as the other. The market value per share is not affected by the payout ratio when **r = k.**

Declining Firms, r < k:

Firm having **r < k** may be referred as declining firm. The optimum payout ratio for a declining firm is 100%. The market value per share, P, increases as payout ratio increases as pay out ratio increases when **r < k**.

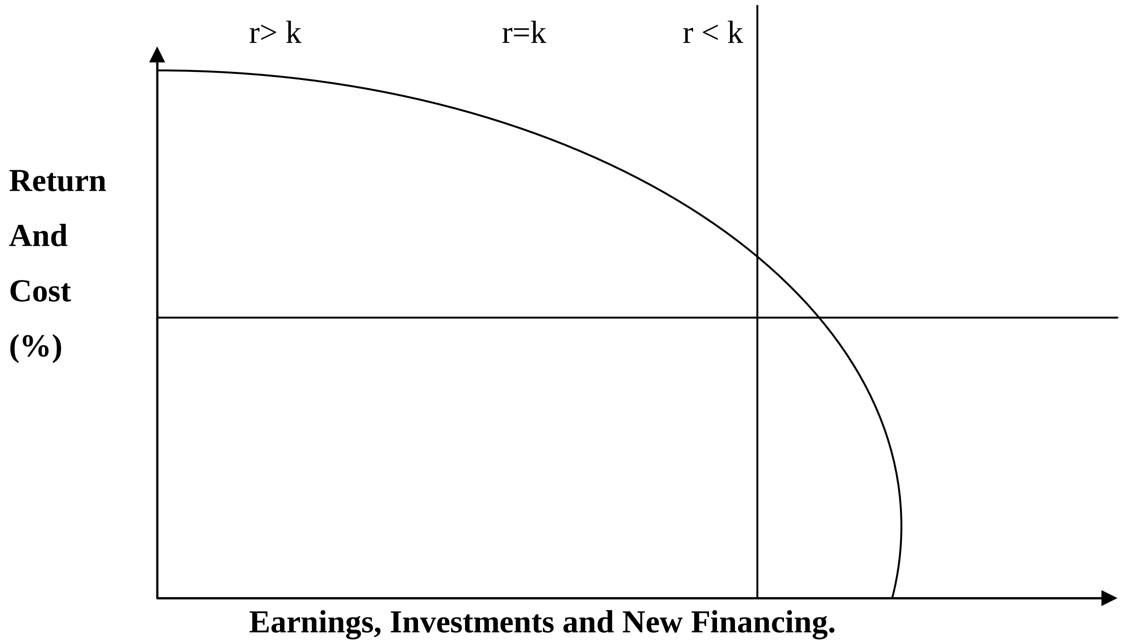


Fig: Earning, Investment and New Financing Under Walter's Model

Thus, in Walter's model, the dividend policy of the firm depends on the availability of investment opportunities and the relationship between the firm's internal rate of return r and its cost of capital (k). The firm should use earnings to finance investments if r > k; should distribute all earnings when r<k and would remain indifferent when r = k. Thus, dividend policy is a financing decision. When dividend policy is treated as a financing decision, the payment of cash dividends is a passive residual (Soloman, 1963:130 -140).

Gordon's Model:

Myron Gordon develops one very popular model explicitly relating the market value of the firm to dividend policy. Myron Gordon made a study on the dividend policy and market price of the stock and concluded that the dividend policy of the firm influences the market value of Stock. This is a relevant theory similar to the Walter's model. In the study conducted in 1953, he explained, "The investors prefer present dividend rather than future capital gains". He further explained that the dividend policy has direct relationship with the value of stock even if the internal rate of return is equal to required rate of return.

Gordon's model is based on the following assumptions (Pandey, 1995:745-746):

- The firm is an all- equity firm.
- No external financing is available. Consequently retained earnings would be used to finance any expansion.
- The internal rate of return, r, of the firm is constant. This ignores the diminishing marginal efficiency of investment.
- The appropriate discount rate k for the firm remains constant. Thus, Gordon's model also ignores the effect of a change in the firm's risk-class and its effect of k.
- The firm and its stream of earnings are perpetual.
- The corporate taxes do not exist.
- The relation ratio b, once decided upon, is constant. Thus the growth rate, g = br is constant forever.
- K >br = g. If this condition is not fulfilled, we cannot get a meaningful value of the share.
- According to Gordon's dividend capitalization model, the market value of share is equal to the present value of an infinite stream of dividend to be received by the share.

Thus,

$$P_o = \frac{D1}{(1+K)^1} + \frac{D2}{(1+K)} + \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots.. + \frac{Dn}{(1+K)^n}$$

Gordon has further developed the following equation for the computation of market value of stock:

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

Where,

P = Market Price per Share

EPS = Earning per Share.

b = Retention ratio.

ke = Cost of Capital.

1-b = Payout ratio.

br = Growth rate.

Gordon’s relevant theory is a popular theory of dividend. As investors prefer current dividend earnings rather than expected higher future income so as to eliminate the risk associated with future capital gain. Gordon stressed that the higher payout increases the dividend yield and hence increases the value of stock. But the assumption of this model is also far from the reality.

Modigliani and Miller’s Model:

According to Modigliani and Miller (M-M), dividend policy of a firm is irrelevant. As dividend policy does not affect the wealth of the shareholder. They argue that the value of the firm depends on the firm’s earnings, which result from its investment policy. Thus, 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 the firm. M-M’s hypothesis of irrelevance is based on the following assumptions (Pandey, 1995: 751-752):

- The firm operates in perfect capital markets where investors behave rationally, information is freely available to all the transactions and flotation costs do not exits. Perfect capital markets also imply that no investor is large enough to affect the market price of a share.
- Taxes do not exist; or there are no differences in the tax rates applicable to capital gains and dividends. This means that investors value a rupee of dividend as much as a rupee of capital gains.
- The firm has a fixed investment policy.

– Risk of uncertainty does not exist. That is, investors are 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 t.

Modigliani and Miller provide following model to prove their theory (Niroula, 2003:25-26):

Market value of share:

The market value of a share at the beginning of the period is equal to the present value of dividend paid at the end of the period plus the market price of the share at the end of the period. Symbolically,

$$P_o = \frac{D_1 + P_1}{1 + K_e} \text{ ………………….. (i)}$$

Where,

P_0 = Market price of share at the beginning of the period.

D_1 = Dividend per share at the end of the period.

P_1 = Market price per share at the end of the period.

K_e = Cost of equity capital

No external financing:

If no new external financing exists the market value of a firm can be computed by multiplying both sides by the number of outstanding shares follows:

$$nP_O = \frac{n(D_1 + P_1)}{1 + K_e} \text{ ……………………………..(ii)}$$

Where,

n = Number of outstanding shares.

New Shares:

If retained earning is not sufficient to finance the investment opportunities. Issuing new shares is the other alternatives. Assuming that m is the number of newly issued equity share at the price of P1, the value of firm at time 0 will be:

$$np_o = \frac{nD1 + P1(n+m) - mp1}{1 + k_e} \text{ ………………………………(iii)}$$

Where,

n= Number of shares at the beginning.

m= Number of shares issued at the end of the period.

Total numbers of shares:

A firm can pay dividends and funds to undertake the optimum investment policy. If the firm finances all investments opportunities either by issue of new equity of retained earnings, the total numbers of new shares can be computed on the following way:

$MP_1 = I - (E\text{-}Nd_1)$ ……………………………….(iv)

Where,

MP1= Amount obtained from the sales of new shares.

I= Amount required for new investment during the period.

E= Total earning the period.

$E - Nd_1$= Retained earning.

$_{Nd1}$= Total dividend paid.

Substituting the value of Mp1 of equation (IV) to equation (III) we get.

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

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

A firm, which pays dividends, will have to raise funds externally to finance its investment plans. M-M's argument, that dividend policy does not affect the wealth of the shareholders, implies that when firm pays dividends, external financing offsets its advantage. This means that the terminal value of the share declines when dividends are paid. Thus, the wealth of the shareholders – dividends plus terminal price – remains unchanged. As a result, the present value per share after dividends and external financing is equal to the present value per share after dividends and external financing is equal to the present value per share after dividends and external financing is equal to the present value per share before the payment of dividends. Thus, the shareholders are indifferent between payment of dividends are retention of earnings (Pandey, 1995: 753-754).

M-M asserts that their hypothesis of dividend irrelevance is not affected if the firm raises external funds by issuing debt instead of Shares. When external financing involves debt M-M invoke their indifference hypothesis with respect to leverage (Pandey, 1995:754).

Pradhan's Study (1993, Vol. IX)

Dr. Radhe S. Pradhan studied the market behaviour of the stock in Nepal in 1993. In his study titled **"Stock Market Behaviour in Small Market"** studies the data were collected from 17 enterprises covering the years 1986 to 1990. His conclusion can be listed below:

- There was higher liquidity on stock with larges ratio of dividend per share to market per share.
- There was lower language ratio on stocks with large ratio of dividend per share to market per share.
- There was higher earning on stock with larger ratio of dividends per share to market per share.
- Ratio of dividends per share to market price per share was positively correlated.
- There was positively relationship between dividends pay out with liquidity ratio and profitability.
- The relationship between dividend payouts and turnover ratio was observed to be positive.
- Dividend payouts and interest coverage were positively correlated.

Although, Pradhan's study is considered as a landmark study in the field of dividend policy in Nepal. It was conducted more than a decade ago when the Nepalese capital market was in an infant stage. However, with the passage of time Nepalese capital market has come long way towards perfection. So, it can be said that the result depicted from his study may not be relevant today and a new study is necessary. Moreover, he has not calculated the test of hypothesis, especially ANOVA test. Therefore, whether the financial indicators such as EPS, DPS and DPR results obtained values are significant or not, can not be said and hence the validity of the result is doubtful.

Shrestha and Manandhar's Study (Year1998; Vol.: VIII)

Professor M. K. Shrestha & K. D. Manandhar conducted empirical study on **"Bonus share issue practices in Nepalese corporate firms"**. The study is concentrated on factual analysis of the prevailing practices among Nepalese corporate firm regarding the issue of bonus shares. Besides issue of bonus share is characterized by ad-hocism and imperfect and under- developed capital market, the study fulfils the research gap and add inputs to financial literature relating to this topic.

The period of study expands over ten years from 1988/89 to 1997/98. The study includes the bonus share issue by the sample corporate firms, which had issued the bonus share at least once during the study period. There are a total of 36 bonus issues amounting to Rs.951.8 million for the period under study.

They used simple statistical tools to analyze and interpret the data. Used statistical tools are percentage, frequency distribution and average.

Their main objectives of the study are as follows:

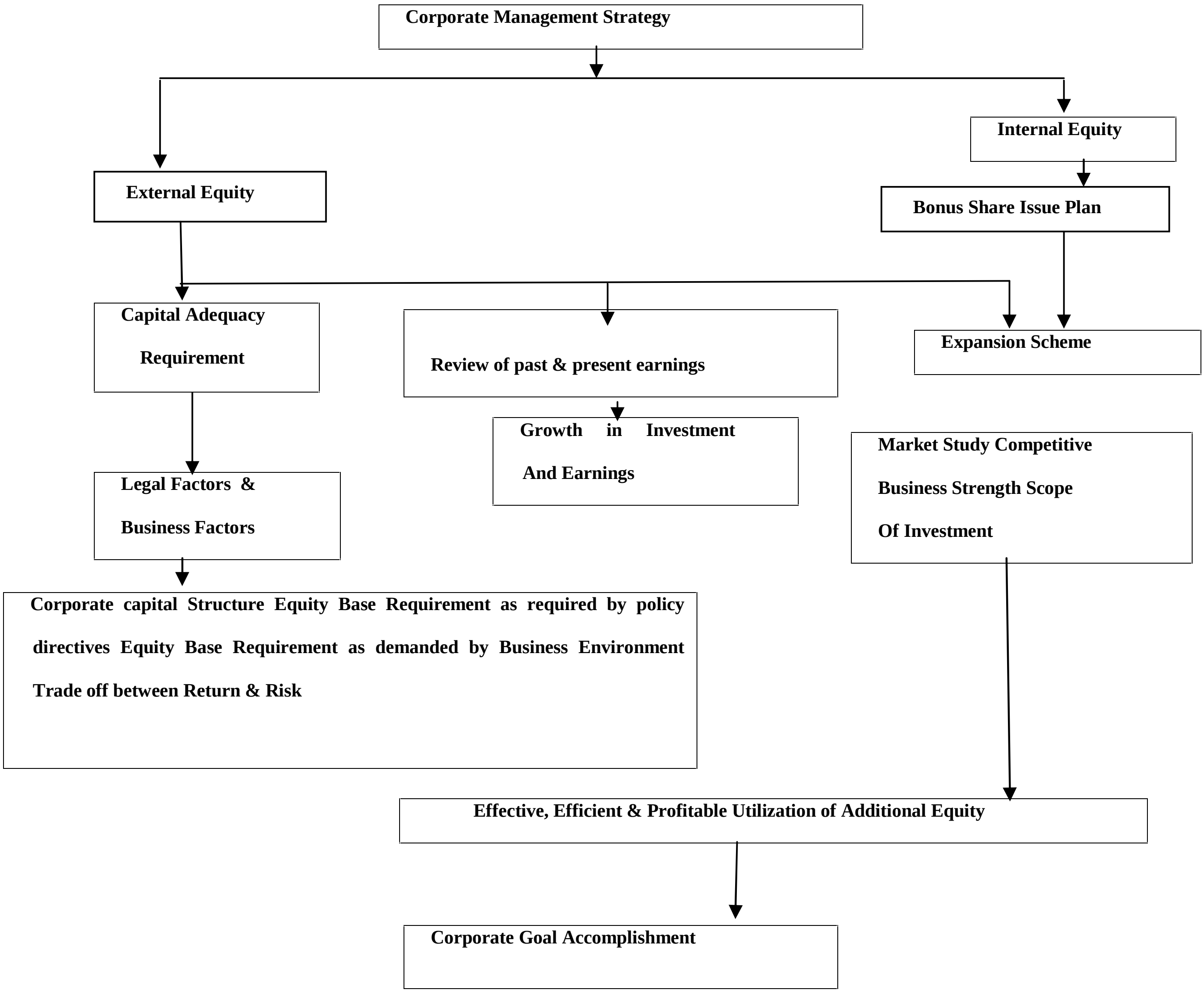
- To study and analyze the frequency of bonus share issue.
- To study and analyze the regularity of bonus share issue.
- To identify the most popular bonus share issue ratio.
- To study and analyze the relation of bonus share issue to the size and age of the corporate firms.

The study's selected samples are related to commercial banking, Insurance, Finance, Trading and Service sectors. On the base of analysis of 12 bonus issuing corporate firms, following findings were observed on the bonus share issue practices in Nepal:

- The most popular bonus ratios prevalent in Nepalese corporate practices are 1:2, 1:1 and 1:5. But 1:2 ratios overwhelmingly dominated.
- The number of bonus issue tended to rise from 1992 /1993 and enthusiastic increase in number of bonus share issue in the fiscal year 1994 /95.
- The amount of bonus issue showed increasing trend during the period of study.
- There is a trend to raise the additional equity capital by capitalization the reserves and net profit by issuing bonus share and stock dividend.
- In the later years the importance of 1:2 bonuses decreased and importance of other ratios less than 1:2 increased which are 1:5 and 1:4.The ratio bonus share is considered high as compared to widely prevalent practice in American corporate.
- The overall average of 3 bonus issues is noticed among Nepalese corporate practice during the study period.
- Nepalese corporate firms are found depended in internal equity rather than external equity for additional capital.
- There is no consistency in bonus issue ratio is observed among Nepalese corporate firms.

- Though capitalizing the retained profit by issuing the bonus shares is the prevalent practice, the average growth rate in increase in equity capital between the commercial banking group and non-banking group differed widely.
- The large corporate firms are found to issue bonus shares more ties than the small size corporate firms.
- Corporate firms over than 20 years are found to have issued bonus share more times compared to other corporate firms will lesser age.

Based on the study and analysis the model suggested for bonus Share issue is given below:



Mandandhar's Study (2000, Vol 10)

Dr. Kamal Das Manandhar conducted a study titled **"Preliminary Test of Lagged Structure of Dividends, Empirical Test Case of Corporate firms in Nepal"** to test the lagged structure of dividend and different hypothesis on relationship of dividend payout and other financial factors were tested. He carried out his study based on the data taken from Nepalese corporate firms and covered the period of 1987 to 1998. The conclusions for his study are as follows:

- There is significant relationship between changed in dividend policy in terms of DPS and change in lagged earnings.
- There is relationship between distributed lagged profits and dividends.
- In overall there is a positive relationship between changed in lagged consecutive earnings and dividend per share.
- When change in lagged consecutive earnings is greater than zero, in 65% cases, change in DPS.

Batchelor and Orakcioglu's Study:

Professor Roy Batchelor and Ismail Orakcioglu did a study of **"The impact of Stock dividends in Turkey".** In this study, they examines the behavior of the prices of leading share traded on the Istanbul Stock Exchange (ISE) in the weeks before and after the payment of stock dividends. They apply an event study methodology using pooled cross-sectional and time series data, with the novel twist that price movements through the event window are assumed to follow a mixture of GARCH process. Which allows to mature and test the significance of stock dividends for both the level and volatility of share prices, and to control for the effects of the simultaneous payment of cash dividends?

Major findings of the study:

- In Turkey, almost all major listed companies, regardless of performance, split their stock
- Each year by means of stock dividends, which are typically paid alongside cash dividends and often company a right issue.

- There are not significant effects on returns from stock dividends either before or after their payment, but very large price volatility on the ex-dividend day. Presumable reflecting investor confusion as to proper post-split value of the share.
- Real increases and decreases in cash dividends do cause returns to rise and fall after the dividend payment date rather than after the earlier announcement date and we find evidence that firms and investors treat cash and stock dividends as substitutes. This suggests some degree of money illusion and irrationality in market reactions to dividend payments on the ISE.
- There is a very strong association between rights issues and stock dividends. Which suggests that stock dividends are used by companies in hope of reducing the apparent price to shareholder of the new stock?
- Stock dividend payments on the ISE are not motivated by the same factors- such as past or prospective out performance – which trigger stock splits in more developed markets. They are largely driven by accounting and regulatory considerations. However, the presence of stock dividend payments on the ISE do appear to lead investors to behave irrationally, to treat the stock dividends as substitutes for cash dividends and as an effective discount on the price of rights issues.
- Cash dividend payments do have a significant impact on excess returns. There is no systematic movement in price in the weeks before the dividend payment date. But after the dividend date, the price of shares, which pay and improved dividend rise and the prices of shares, which pay a lower dividend, falls.

2.4. Review of Previous Research

Timilsina's Study (1997)

MBA Thesis entitled **"Dividends and Stock Prices: An Empirical Study"** conducted by Mr. Sadakar Timilsina was carried out by using the data of 16 enterprises for the period of 1990 to 1994.

Objectives of the Study are as follows:

- To test relationship between DPS and Stock Prices.
- To determine the impact of dividend policy on Stock prices.
- To identify whether it is possible to increase the market value of the Stock changing dividend policy or payout ratio.

- To explain the behaviour, he used multiple regression models of three independent variables as developed by Friend and Puckett. Further he tried to highlight the relationship between stock price and other independent variables setting separate simple linear regression equations. The findings of the study are as follows:
- To study the prevailing practices and efforts made in dividend policy in the Nepalese firms with the help of sample firms.
- To find out the impact of dividend policy on market price of stock.
- To analyze if there is any uniformity among DPS, EPS, MPS and DPR in the sample firms.

Major findings of his study are as follows:

- There is not any consistency in dividend policy in the sample firms. It was indicated the need of dividend strategy as well as the need of proper analysis of the respective sector of the firms.
- Most of the Nepalese firm from the very past did not have profit planning and investment strategy, which has imbalanced the whole position of the firms. It means there is no consistency even in the earnings.
- The MPS is affected by the financial position and the dividend paid by the firms, in this regards the MPS of the sample firms is seem to be fluctuated. It denotes that Nepalese investors are not treated fairly.
- The lack of financial knowledge and the market inefficiency has affected the market price of the share in all the firms.

Khatiwada's Study (2001)

An MBA Thesis conducted by Mr. Narayan Prasad Khatiwada in 2001 entitled **"Impact of Dividend and Earning Announcement on Shareholder's Return and Stock Prices in Nepal"** collected the data six joint venture commercial banks. The study carried out with the following objectives:

- To analyze the impact of earning and dividend announcement on Shareholders return.
- To identify the correlation between the return of individual securities with market return.
- To identify the quantity of systematic and unsystematic risk.

Some of the major findings of the study were as follows:

- Announcement of dividend and earning do not affect the shareholder's return in average.
- Other banks except Nepal SBI Bank having different dividend rates did not provide significant abnormal return to the shareholders.
- Shareholders realized positive abnormal return from half of the sample banks.

Manadhar's Study (2002)

In 2002 K.D. Manandhar studied on **"Corporate dividend policy and Practice in Nepal"** The study has gone in depth about all form of dividend that is practiced in Nepal. This study presents study and analysis of Bonus Share issue practice of corporate firms in Nepal as the Bonus Share is in important form of dividend. The study has covered the period of 1987/88 to 1997/98, and included 36 no. of bonus share issued during the period. The study deals with the following aspects.

- Conceptual framework of Bonus Share issue.
- Legal and procedural aspect of Bonus Share issue.
- Review of relevant studies relating to the Bonus Share.
- Characteristics feature of Bonus Share issue practice of corporate firms in Nepal.
- Effects of Bonus Share issue on dividend.
- Effect of Bonus Share issue on Market price of Share.

Some of the major findings of the study were as follows:

- The study reveals that Nepalese Corporate firms, to a great extent relied on issue of Bonus
- Share in increasing their equity capital base.
- The study found that large corporate firms in general trend to issue Bonus Shares in higher ratios as compared to the small corporate firms.
- There seemed to have been no regular and consistent policy regarding Bonus Share issue in terms of Bonus Ratio and time interval between one Bonus issue and another.
- The fact that after Bonus Share issue, the dividend rate increased did not seem to be universally true as approximately only 50% of the cases after the Bonus issue, dividend rate increased.

- There is not immediate price rise significantly after Bonus Share issue as expected. Market price start rising after 6 month form the announcement date.
- Nepalese Corporate listed Share price can be maximized if corporate management announces the Bonus Ratio to the maximum of 1:1.
- The most practiced form of dividend in Nepal is Cash dividend.

Gharti's Study (2001)

Mr. Padam Gharti conducted a **"Bonus share announcement and its impact on stock price of Nepalese corporate firms"** by using secondary data of 10 percent firms.

Objectives of the study are as follows (Gharti, 2001):

- To examine the relationship of dividend quantum change and stock price.
- To examine the relation between share price and bonus ratio.
- To evaluate the relation of bonus share announcement and stock price.
- To point out suggestions to the related bodies.

Major findings of the study are as follows:

- The immediate share price rise after bonus announcement is significant. Bonus share announcement of banking sector is considering positively by the investors but shows reluctant for the non-banking sectors. None of the case has been observed under banking sector that the price decreases immediately after bonus announcement.
- The intention of issue bonus share of board of directors leaks out before officially announcement. Therefore, the share price rises one month before the actual announcement due to the activities of the 'insiders'.
- The share price, in most of the case, does not decrease after distribution of bonus share outstanding to bonus ratio as theory says. The reason behind the situation may be that the investors cannot interpret the information and data. There is a great misconception about bonus share that the general investors think that they receive extra / additional share with same value.
- The share price of the non-banking sectors shows inconsistency as companies to the banking sector. Therefore investing on non-banking sector is more risky than the banking sector.
- Long –term effect of bonus share issue, as well as immediate, is significantly positive. In most of the cases the aggregate market value of the corporate firms'

equity capital increased as the result of bonus issue. 81.2 % of the bonus issue cases are recorded different level gain over the base data price, after adjustment of the general market movement in share prices.

Koirala's Study (2006)

Mr. Dharma Raj Koirala prepared an MBS thesis entitled **"Bonus share issue practice of corporate firms in Nepal and its impact on MPS"** with data taken from all stock dividends from 1999/2000 to 2003/2004 listed in NEPSE. He analyzed the data of 5 – years from 1995 to 2000 of 16 corporate firms.

The main objectives of the Study are as follows:

- To examine the relationship between bonus share and Stock prices.
- To analyze and test the feedback of the opinion survey relation to the Shareholders preferences as regard to bonus share issue of corporate firms.
- To know the Bonus Share issue practices in related Corporate Firms.
- To remove some of the widely – held misconception about Bonus Share.
- To point out suggestions and recommendation to the related bodies.

Major Findings of this study are as follows:

- The practice of Bonus Share issue is in increasing trend per year, so far bonus share has been issued 41 times under the study period.
- The Share prices are decreased after the bonus share issue in all cases but sometimes Share price increased.
- Corporate firms specially, financial sector in Nepal have practice of issuing bonus share to increase the total capital fund.
- The popular dividend rate of Nepalese Corporate Firm is 20% listed companies have issued 9 times in last 5 Years.
- The minimum Stock dividend rate is 10% in Nepal.
- Manufacturing, Trading and Development Bank are not issuing bonus share in last 5 Years.
- A Share price in most cases does not decrease after bonus share issue as Theory says. The reason behind the situation may be that investors cannot interpret the information on the data.

– Most Companies Market price of Share does not decrease as the same percentage as stock dividend rate. This means investors are positive towards those companies issuing bonus share.

Pathak's Study (2008)

Mr Binod pathak prepared an MBS thesis entitled "**Bonus share practices in Nepalese corporate firm"** where he has analysis 50 corporate firms out of which 11 banks, 24 finance, 7 insurance, 2 hotels and 1 manufacturing sector .His study is based on data from 1994 to 2007/2008.

The main objectives of the Study are as follows:

- To examine and study the present practice of issue of bonus share in Nepalese corporate firms.
- To study the impact of bonus share in secondary market.
- To study the investor's attitude about bonus share.
- To provide suggestion on the basis of major finding**.**

Major Findings of this study are as follows:

- The practice of bonus share issue in Nepalese corporate firms is not regular and consistent.
- In Periodic trend, the amount of equity share capital before each bonus issue are increasing trend but the average ratio of bonus issue to equity capital is in decreasing trends.
- In frequency of bonus issue ,total 50 corporate firms issued 122 bonus share .Among them 1 company issued 6 times ,2 companies issued 5 times, 3 companies issued 4 times ,1 company issued 10 times , 1 company issued 8 times ,6 corporate firms issued 3 times,22 companies issued 2 times and 14 companies issued 1 time bonus share
- The immediate impact on combined market price of stock due to the bonus issued announcement is negative i.e. market price decrease by 2.87% but not in the ratio of theoretical value.

Pandey's Study (2008)

Ms Prakrity Pandey prepared an MBS thesis entitled **"Bonus share issue practice of corporate firms and its impact on MPS"** with data taken from all stock dividends from 2001/2001 to 2004/2005 listed in NEPSE by analysing 31 corporate firms.

The main objectives of the Study are as follows:

- Corporate Management's opinion and attitude in regards to bonus share issue and practice.
- To do an empirical study on the shareholder's perception on bonus share issue and shareholder's dividend behaviour.
- To remove some of widely held misconception about bonus share.

Major Findings of this study are as follows:

- The practice of bonus share issue is in increasing trend per year, during the study period bonus share has been issued for 52 times while in the year 2006, 22 corporate firms issued bonus share for the fiscal year 2004/2005.
- The share price is decreased after the bonus share is issued in all cases but sometime share price is found increased in rare case.
- Manufacturing & Trading firms are not issuing bonus share in last 5 year due to high rate of inflation, political instability, Maoists insurgency & low economic growth.
- The actual market price & theoretical market price is not equal in the above table which means there is fluctuation in market price after issuance of bonus share.
- Most corporate firm's market price of share does not decrease as the same rate of stock dividend. This may be due to small knowledge of investors being immature market and the next reason could be investor's perception towards the corporate firm issuing bonus share is positive in stock market.

Pandey's Study (2008)

Mr Sanjiv Pandey an MBS student has prepared a thesis entitled on "**Effect of right share and bonus share on market price".** (with reference to Nepalese bank and financial institution) where he has focus on the effect of right share and bonus shares to market price after announcement of issue of right and bonus share and its price movement on Nepal stock exchange on sample basis. He has taken two banks i.e. Nepal

Industrial and Commerce Bank Ltd and Nepal SBI Bank and two finance i.e. Peoples Finance and Siddhartha Finance. His studies is based on the data from 2058 to 2063

The main objectives of the Study are as follows:

- To examine and analyse various aspects of bonus share and right share.
- To evaluate the effect in Market Price Per Share allotment of right share and bonus share.
- To evaluate the problems regarding to investors in associates with right share and bonus share ,
- To suggest and recommend on the basis of major finding.

Major Findings of this study are as follows:

- There is significant change in the share price after the announcement of right and bonus share
- Under subscription of right and bonus share issued lack of effectiveness in the flow of information.
- Most company announce the bonus share to show the positive impact in investors.
- The regulation is not clear and the process of approval is lengthy regarding right share and bonus share issue.

2.5 Research Gap

Various studies have been made under bonus share and have found different things. Till date many researchers are involved to find out the exact reason why bonus share is affecting the MPS. Theory of bonus share emphasizes on decrease of share price after the announcement of bonus share by a corporate firms but in reality it’s not so. The investors of our immature stock market are not able to interpret the right information of the data provided by the stock market. That’s why some of the investors are playing on speculative way.

Hence, as per my objective I want to analyze & examine the bonus share effect of stock market, how they change? By examining the relation of dividend quantum with change in stock price, we derive whether the change of stock price is reasonable or not. This research studies the existing situation of bonus share issue practice of corporate firms in Nepal & whether they are considering the issue of bonus share as a crucial matter or not.

This research also covers the shareholders opinion & views on bonus share, how they perceive it and also the corporate management's opinion & attitude. This research also includes an empirical study on shareholders perception on bonus share issue & shareholders dividend behaviour.

As, bonus share announcement is taken as a positive signal by an investors in reality it is a reshuffle of the capitalization in the equity portion of the balance sheet. So, this research helps to remove some of widely held misconception about bonus share and also provides suggestion & recommendation to the related body.

CHAPTER - III

RESEARCH METHODOLOGY

3.1 Introduction

Research design refers to the entire process of planning and carrying out a research study. Identification, selection and formulation of a research problem may be considered as the planning stage of a research. The remaining activities refer to the designs, operation and completion of the research study. (Wolf and Pant, 1999: 203). Research methodology is a way for systematically solving the research problem. In other words, research methodology indicates the methods and process employed in the entire aspects of the study.

Research design is the way to subsequently solve the research problem (Kothari, 1990:10). It describes the method and process applied in the entire aspect of the study. A focus is given to the nature and source of data, the model statistical tools used, and limitations of the study.

In order to achieve the objective of the study an appropriate methodology becomes necessary, which is an essential part of study throughout the study. Thus, this study consists of research design, population & sample, nature and sources of data, data processing procedure and method of analysis.

A systematic research design is necessary to fulfil the objective of study. It means defined procedures & techniques that guide and propounds ways for research viability. Several typologies have been suggested for classifying a wide variety of research designs according to nature of research. This study is not an experimental one. To facilitate the assessment, we collected bonus share announcements within five years and related share prices and are tabulated, manipulated and analyzed according to needed results.

Where as, this is a casual comparative research, which investigates the possible causes affecting a particular situation by observing existing consequences and searching for the possible factors leading to these results. This research is ‘ex past facto’ in nature.

3.2 Population & Sample:

The data collection activity consists of taking ordered information from reality and transferring it into some recording system so that it can later be examined and analyzed for patterns. Population or universe refers to the entire group of people, events or things of interest that the researcher wishes to investigate. In most of cases, we are not able to collect data of whole population or universe (an aggregate of the set of result of an operation). Bonus share issue is a recent phenomenon in Nepalese corporate firms. It came into practice after the incorporation of joint venture banks in mid-eighties as a result of Government's economic liberalization policy. As we well know the drawbacks of imperfect & underdeveloped capital market, it is ironically challenging to collect financial data, specially the share price of a particular date.

The analysis of share issue has been regularly practice but due to large data & limited time the study duration is selected of recent five years. Among the samples those corporate firms will be ignored who are not actively trading during the study period. Total population (total commercial bank, finance company and insurance)
who are trading are mentions below:

Table 3.1

Total population of commercial bank

Sn	**Commercial Banks**	**Operation Date(AD)**	**Paid Up Capital (Rs. In Million)**
1	Nepal Bank Limited	1937/11/15	380.4
2	Rastriya Banijya Bank	1966/01/23	1172.3
3	Agricultural Development Bank Limited	1968/01/02	9278.0
4	NABIL Bank Limited	1984/07/16	689.2
5	Nepal Investment Bank Limited	1986/02/27	1002.6
6	Standard Chartered Bank Nepal Limited	1987/01/30	620.8
7	**Himalayan Bank Limited**	**1993/01/18**	**810.8**
8	Nepal SBI Bank Limited	1993/07/07	647.8
9	Nepal Bangladesh Bank Limited	1993/06/05	744.1
10	**Everest Bank Limited**	**1994/10/18**	**831.4**
11	Bank of Kathmandu Limited	1995/03/12	603.1
12	Nepal credit and commerce Bank Ltd	1996/10/14	1195.7

Sn	Commercial Banks	Operation Date(AD)	Paid Up Capital (Rs. In Million)
13	Lumbini Bank Limited	1998/07/17	750.0
14	**Nepal Industrial and Commercial Bank Limited**	**1998/07/21**	**792.0**
15	Machhapuchhre Bank Limited	2000/10/03	821.7
16	Kumari Bank Limited	2001/04/03	900.0
17	Laxmi Bank Limited	2002/04/03	732.0
18	Siddhartha Bank Limited	2002/12/24	690.0
19	Global Bank Limited	2007/01/02	700.0
20	Citizens Bank International Limited	2007/06/21	560.0
21	Prime Bank Limited	2007/09/24	700.0
22	Sunrise Bank Limited	2007/10/12	700.0
23	Bank of Asia Nepal Limited	2007/10/12	700.0
24	Development Credit Bank Ltd	2001/01/23	301.00
25	NMB Bank Ltd	1996/11/23	1000.00
26	Kist Merchant Banking and Finance Ltd	2003/02/21	2000.00

Source:www.nrb.org.np

Table 3.2

Total population of Finance companies

Sn	Finance Companies	Operation Date(AD)	Paid Up Capital (Rs. In Million
1	Nepal Housing Development Finance Co.Ltd.	1992/03/08	145.0
2	Nepal Finance Co.Ltd.	1993/01/06	67.5
3	NIDC Capital Markets Ltd.	1993/03/11	101.2
4	**National Finance Co.Ltd.**	**1993/05/07**	**217.4**
5	**Annapurna Finance Co.Ltd.**	**1993/09/30**	**262.1**
6	Nepal Share Markets and Finance Ltd.	1993/10/19	432.0
7	Peoples Finance Ltd.	1993/04/15	202.1
8	Mercentile Finance Co. Ltd.	1994/11/10	18.0
9	Kathmandu Finance Ltd.	1994/11/10	75.9
10	Himalaya Finance Co.Ltd.	1993/11/11	48.0
11	Union Finance Ltd.	12/12/1995	159.9
12	Narayani Finance Ltd.	1995/03/08	213.7
13	Gorkha Finance Ltd.	1995/03/12	59.6
14	Paschhimanchal Finance Co.Ltd.	1995/04/09	100.0
15	Nepal Housing & Merchant Finance Co.Ltd.	1995/04/11	160.7
16	Universal Finance Co.Ltd.	1995/04/27	131.4
17	Samjhana Finance Co. Ltd.	1995/05/03	72.7
18	Goodwill Finance Ltd.	1995/05/16	115.5

Sn	Finance Companies	Operation Date(AD)	Paid Up Capital (Rs. In Million
19	Siddhartha Finance Co. Ltd.	1995/05/25	86.9
20	Shree Investment & Finance Co. Ltd.	1995/06/01	100.8
21	Lumbini Finance & Leasing Co. Ltd.	1995/06/26	120.0
22	Inbesta Finance Ltd.	1995/07/17	24.0
23	Yeti Finance Co. Ltd.	1995/07/23	62.5
24	Standard Finance Ltd.	1995/07/23	667.9
25	International Leasing & Finance Co. Ltd.	1995/10/31	648.0
26	Mahalaxmi Finance Co. Ltd.	1995/11/26	116.0
27	Lalitpur Finance Co. Ltd.	1995/12/12	113.9
28	Bhajuratna Finance & Saving Co. Ltd.	1996/01/09	38.5
29	**United Finance Ltd.**	**1996/1/25**	**165.0**
30	General Finance Ltd.	1996/02/02	24.2
31	Nepal Shreelanka Merchant Bank Ltd.	1996/02/04	100.0
32	Merchant Finance Co. Ltd.	1996/01/02	33.4
33	Alpic Everest Finance Ltd.	1996/07/16	102.9
34	Nava Durga Finance Co.Ltd.	1997/02/09	45.6
35	Janaki Finance Ltd.	1997/03/07	50.0
36	Pokhara Finance Ltd.	1997/03/16	60.0
37	Central Finance Co. Ltd.	1997/04/14	126.9
38	Premier Finance Co. Ltd.	1997/05/08	97.1
39	Arun Finance & Saving Co. Ltd.	1997/08/17	11.0
40	Multipurpose Finance Co. Ltd	1998/3/25	6.0
41	Butwal Finance Co. Ltd.	1998/06/21	97.7
42	Shrijana Finance Ltd.	1999/12/14	28.0
43	Om Finance Ltd.	2000/09/17	105.0
44	Cosmic Merchant Banking & Finance Ltd.	2000/11/20	75.1
45	World Merchant Banking & Finance Ltd.	2001/08/10	72.0
46	Capital Merchant Banking & Finance Ltd.	2002/02/01	374.0
47	Crystal Finance Ltd.	2002/02/13	49.0
48	Royal Merchant Banking & Finance Ltd.	2002/02/14	134.3
49	Guheshworil Merchant Banking & Finance	2002/06/13	109.8
50	Patan Finance Ltd.	06/23/2002	50.0
51	Fewa Finance Ltd.	2003/04/30	91.0
52	Everest Finance Co. Ltd.	2003/07/02	20.0
53	Birgunj Finance Ltd.	09/28/2003	180.8
54	Prudential Bittiya Sanstha Ltd	2003/06/06	100.0
55	ICFC Bittiya Shanstha Ltd.	2003/06/15	299.4
56	IME Financial Institution Ltd.	2005/08/01	249.5
57	Sagarmatha Merchant Banking and Finance Co.	2005/08/29	50.0
58	Shikhar Bittya Sanstha Ltd.	2005/09/15	50.0
59	Civil Merchant Bittiya sanstha Ltd.	2005/09/18	80.0
60	Prabhu Finance Co. Ltd.	2006/02/16	160.0
61	Imperial Finance Ltd.	2006/03/08	100.0

Sn	Finance Companies	Operation Date(AD)	Paid Up Capital (Rs. In Million
62	Kuber Merchant Bittiya sanstha Ltd.	2006/03/24	81.2
63	Nepal Express Finance Ltd.	2006/05/04	98.3
64	Valley Finance Ltd.	2006/05/11	27.5
65	Seti Bittiya sanstha Ltd.	2006/06/07	5.2
66	Hama Merchant & Finance Ltd.	2006/06/16	82.9
67	Reliable Finance Ltd.	2006/09/06	121.1
68	Loard Buddha Financial Institutions Ltd.	2006/11/19	75.0
69	Api Finance Ltd.	2007/4/25	60.0
70	Nameste Bitiya Sanstha Limited.	2007/07/07	10.1
71	Kaski Finance Limited	2007/7/30	50.0
72	Suryadarshan Finance Co. Ltd.	2007/7/30	30.0
73	Zenieth Finance Ltd.	2007/10/08	63.0
74	Unique Financial Institution Ltd.	2007/10/12	60.0
75	Manjushree Financial Institution Ltd.	2007/10/15	70.0
76	Swostik Merchant Finance Company Ltd.	2007/10/16	34.8
77	Subhalaxmi Finance Ltd.	2007/11/11	70.0

Source:*www.nrb.org.np*

Table 3.3

Total population of Insurance Companies

Sn	Insurance Companies	Operation Date(AD)
1	Nepal Insurance Co Ltd	1947/09/24
2	The oriental Insurance Co Ltd	1967/09/15
3	Rastriya Beema Sanstha	1968/12/15
4	National Insurance Co Ltd	1974/01/01
5	National Life Insurance Co Ltd	1988/01/07
6	Himalayan General Insurance Co Ltd	1993/07/21
7	United Insurance Co Ltd	1993/10/22
8	Premier Insurance	1994/04/21
9	**Everest Insurance Co Ltd**	**1994/05/31**
10	Neco Insurance Ltd	1996/05/30
11	Sagarmatha Insurance Co Ltd	1996/06/26
12	**Alliance Insurance Co Ltd**	**1996/07/19**
13	N. B. Insurance Co Ltd	2001/01/23
14	Nepal Life Insurance Co Ltd	2001/04/17
15	American Life Insurance Co Ltd	2001/08/02

Sn	Insurance Companies	Operation Date(AD)
16	Life Insurance Corporation (Nepal) Ltd	2001/08/07
17	Prudential Insurance CO Ltd	2002/05/03
18	Shikhar Insurance Co Ltd	2002/10/04
19	Lumbini Insurance Co Ltd	2005/07/15
20	NLG Life Insurance Co Ltd	2005/10/09
21	Siddartha Insurance Co Ltd	2006/04/05
22	Asian Life Insurance Co Ltd	2008/02/27
23	Surya Life Insurance Co Ltd	2008/03/19
24	Gurans Life Insurance Co Ltd	2008/03/31
25	Prime Life Insurance Co Ltd	2008/05/06

Source:www.bisb.org.np

Since, large number of corporate firms have issued bonus share between 2003/2004 to 2007/2008, so it is not possible to collect all the data of these corporate firms due to various constraint. So, we take only few corporate firms who are actively trading in stock market as a sample data for study which are as follows .Sample are based on those firms who have at least issue bonus share twice during research period. The samples are:

Commercial banks

1. Himalayan bank Ltd
2. Everest bank Ltd
3. Nepal Industrial and Commercial Bank Limited

Finance companies

1. National Finance Co.Ltd.
2. Annapurna Finance Co.Ltd
3. United Finance Ltd.

Insurance Companies

1. Everest Insurance Co Ltd
2. Alliance Insurance Co Ltd

Table 3.4

Bonus Share issue in Sample

Year	2003/2004	2004/2005	2005/2006	2006/2007	2007/2008
Commercial Banks					
HBL	25	20	20	5	15
EBL	-	-	20	30	30
NIC	-	-	20	10	20
Finanace					
NFCL	20	20	10	10	50
AFCL	12	50	60	10	20
UFCL	20	-	-	-	25
Insurance					
AICL	10	10	-	-	-
EICL	100	-*	50	-	12.5

*AGM held for two years in 2005/2006

Source: Annual Report of SEBON

Figure 3.1

Bonus Share issue by Sample Commercial Banks

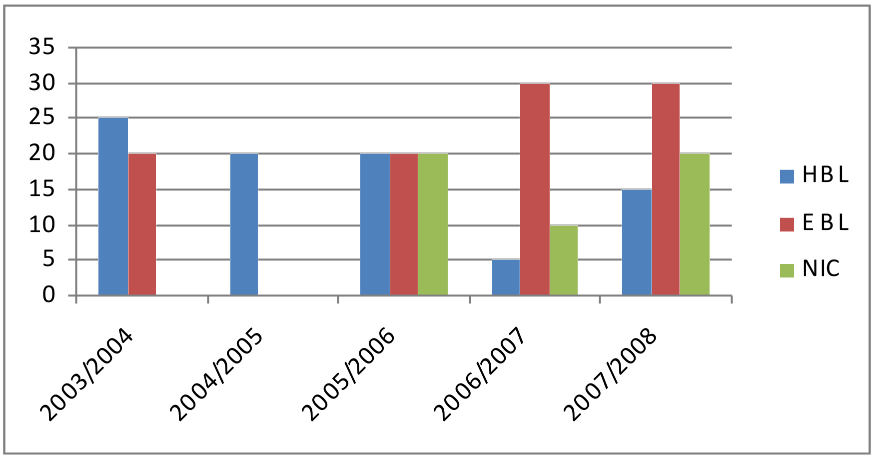


Figure 3.2

Bonus Share issue by Sample Finance companies

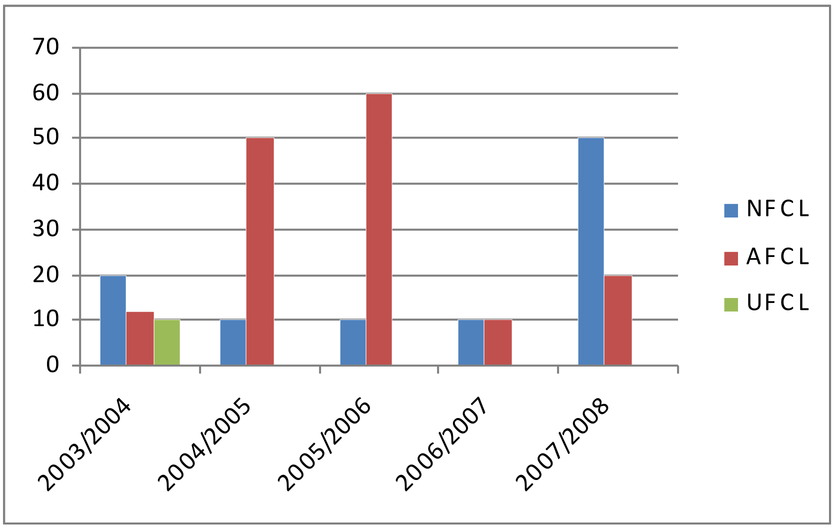
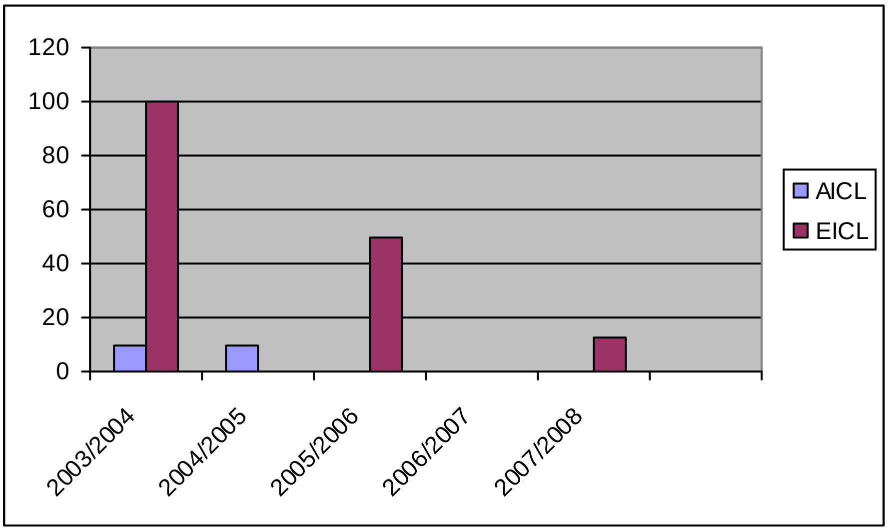


Figure 3.3

Bonus Share issue by Sample Insurance companies



3.3 Nature and Sources of Data:

The data and information in this study are collected from both primary and secondary sources to achieve the real and factual result. Form this research; all the possible and useful data as far as available have been collected. The major sources of data are as follows.

3.3.1 Primary Data

Questionnaires were used as major source to collect primary data for this research. A set of structural questionnaire was made and distributed to the selected respondents in order to get the accurate and actual information from the concerned person. Through questionnaires respondents could tick the right the option or could write their views. Data collected through questionnaire is tabulated and presented in required form to make easy interpretation.

3.3.2 Secondary Data:

Since this study mainly focuses on the data collected through secondary sources. Due to imperfect and underdeveloped financial market, we may not collect all the data only from NEPSE. We were not able to find all the relevant information even in published journals and reports. Therefore, searching the relevant data is an ironical & challenging task. Mainly data were collected from following sources.

- Annual Reports of concerned enterprises.
- Related newspaper and magazines.
- Annual Report and trading Report published by NEPSE.
- Annual Report of SEBON.

3.4 Data gathering Processing

Data and information used in the study are of primary and secondary nature. The secondary data are collected from the publication of SEBON, other journals and related articles. The primary data are collected through the questionnaire. A set of structural questionnaire was made and distributed to the selected respondents in order to get the accurate and actual information from the concerned person. A set of 35 questionnaire was prepared and distributed among the investors out of which 30 respondents replied by filling the questionnaire.

3.5 Data Technique and Tools used

The purpose of analyzing the data is to change it from an unprocessed form to processed & understandable presentations. The collected data need to be aggregated into a form that presents the summary of answers from respondents. The raw data convey little information as such there must, therefore, be compiled, analyzed and interpreted using different data analysis tools (Wolf and Pant, 1999: 247).

In this study, theoretical market price will be used to measure impact of bonus share issue on market price of share. Theoretical market price of share after bonus share issue is given by.

$$= \frac{Before\ Market\ Price\ Pershare - Cash\ Dividend\ Per\ share}{1 + Bonus\ Ratio}$$

(a) Market Price per Share:

MPS is one of the variables, which is affected by stock dividend of the firm. The capital market determines MPS. By using following formula we ca calculate new MPS after stock dividend.

$$P_1 = \frac{P_o}{1 + Bonus\ Ratio}$$

Where,

P_1 = New Market Price of Share. (Theoretical Price)

P_0 = Current Market Price of Share.

(b) Percentage Change in MPS:

The percentage that has been changed in MPS after the bonus share issue is calculated by using this formula.

Percentage Change in MPS = $\frac{MPS_{old} - MPS_{new}}{MPS_{old}}$

Where,

MPS_{old} = Market price of Share before bonus share announcement.

MPS_{new} = Market price of Share after Bonus Share announcement.

(c) Difference in Percentage:

Difference in Percentage is used to analyze difference between two percentages, bonus ratio and percentage change between Theoretical Price and Actual Market Price after bonus share announcement. This formula is used to analyze the difference between two percentages. In this study, this is used to know difference between bonus ratio and percentage change in MPS after the bonus announcement.

Difference in Percentage Bonus Ratio * % Change in MPS

Where,

% Change in MPS = Percentage Change in MPS after the announcement of MPS

(d) Hypothesis

Here,

μ_x = Closing Market Price after Bonus Share issue.

μ_y **= Theoretical Market price after Bonus Share issue.**

Null Hypothesis H_0: $\mu_x = \mu_y$ that is actual Market price after bonus share and Theoretical market price after bonus share issue is same

Alternative Hypothesis H_1: $\mu_x \neq \mu_y$ **(Two tail Test),** that is actual market price after bonus Share is not equal to Theoretical Market Prices after Bonus Share issue.

Test Statistics: Under H_0, the test statistic is:

$$t = \frac{\bar{d}}{\sqrt{\frac{S^2}{n}}}$$

$$\bar{d} = \frac{\sum d}{n}$$

And

$$S_d = \sqrt{\frac{1}{n-1}\sum(d-\bar{d})^2}$$

Where,

d= deviation between Actual Market Price & Theoretical Market price.

$\bar{d}$ = differential Average in between Actual Market Price & Theoretical Market Price.

S_d = Standard deviation

t= Test Statistic

n= no. of Samples

(e) Frequency Distribution

The most widely used method of data analysis and interpretation is frequency distribution. It is used as a method of reporting and summarizing data frequencies simply refer to the number of times various sub-categories of a certain phenomena occurs, from which percentage and accumulative percentage of the occurrence can be easily calculated.

CHAPTER - IV

PRESENTATION ANALYSIS OF DATA

4.1 Introduction

In this Chapter, data collected from Primary and Secondary sources are presented and analyzed. The related data are presented in systematic way in tabular forms and charts. As the bonus share issue in corporate firms is a recent phenomenon so, the characteristics & features issued by the corporate firms of immature stock market are different from those corporate firms issuing bonus share in matured stock market. For the purpose of understanding the several aspect of bonus share issue practice effecting corporate dividend policies and practices, various characteristics of bonus share issue practice of corporate firms of Nepal such as amount of bonus share issue, bonus share issue ratio, the frequency and regulatory of such issue by corporate firms, the relation of bonus issue to the size and age of corporate firms, relation of dividend quantum change & stock price, shareholders' & management perception in issue of bonus share etc. will be studied, examined, analyzed and explained as per the objective of the study. Although the Nepalese capital market has passed more than three decades, bonus share issue is recent practice in Nepalese corporate firms. As per the directive issued by the Nepal Rastra Bank in the fiscal year 2005/06 the issue of bonus share by the corporate firms will increase. The minimum paid up capital to be maintained by the "KA" category (commercial bank) is 2 arab, "KHA" category (development bank) is 64 crore, "GA" category (finance company) who deals in leasing business also are required to maintain 30 crore as paid up capital whereas other finance company has to maintain only 20 crore & other business enterprises of "GHA" category who are engaged in small financial transaction has to maintain 10 crore by the end of Asadh 2070.

4.2 Presentation and Analysis of Secondary Data

The sources of secondary data can be divided into two groups i.e. internal and external. The internal secondary data is found within the company sources, such data includes sales information, accounting data, and trading reports and internally generated research reports. External secondary data are collected from sources outside the corporate firm;

such source may include books, periodicals, published reports, data services and computer data bank. (Wolf & Panta, 2002: 140)

Date of Bonus Share Announcement of Sample Companies:

The day of Annual General Meeting (AGM) is taken as ex-dividend date as in that day issue of bonus share is announced. So, the date of AGM is very important because it is taken as base period for our study in taking stock price before & after announcement of bonus issue.

Table 4.1

Bonus Share Issued by Sample Corporate Firms listed in Nepal Stock Exchange (NEPSE) from period 2003/04 to 2007/2008 with Bonus Ratio.

	AGM	**DATE OF AGM**	**BONUS RATIO**
YEAR(2003/2004)			
Commercial			
HBL	11^{th}	25/03/2004	20
EBL	9^{th}	13/01/2004	-
NIC	6^{th}	05/012003	-
Finance			
NFCL	11^{th}	12/12/2003	20
AFCL	10^{th}	11/01/2004	-
UFCL	9^{th}	05/04/2004	-
Insurance			
AICL	8^{th}	03/04/2004	10
	AGM	**DATE OF AGM**	**BONUS RATIO**
Insurance			
EICL	8^{th} &9^{th}	02/01/2004	100
YEAR(2004/2005)			
Commercial			
HBL	12^{th}	29/12/2005	20
EBL	10^{th}	25/11/2004	-
NIC	7^{th}	03/04/2005	-
Finance			
NFCL	12^{th}	10/12/2004	20
AFCL	11^{th}	11/01/2005	50
UFCL	10^{th}	13/05/2005	-
Insurance			
AICL	9^{th} &10^{th}	03/04/2005	10
EICL	10^{th}	10/04/2005	-

YEAR(2005/2006)			
Commercial			
HBL	13th	10/01/2006	20
EBL	11th	28/11/2005	20
NIC	8th	09/122005	-
Finance			
NFCL	13th	01/12/2005	10
AFCL	12th	11/01/2006	60
UFCL	11th	13/01/2006	-
Insurance			
AICL	-	-	-
EICL	11th	02/04/2006	50
YEAR(2006/2007)			
Commercial			
HBL	14th	11/02/2007	5
EBL	12th	27/11/2006	
NIC	9th	01/12/2006	10
Finance			
NFCL	14th	15/12/2006	10
AFCL	13th	13/01/2006	10
UFCL	12th	12/01/2006	10
Insurance			
AICL	10th &11th	14/01/2006	-
EICL	12th	28/01/2007	-
YEAR(2007/2008)			
Commercial			
HBL	15th	31/12/2007	15
EBL	13th	03/11/2007	30
NIC	10th	14/12/2007	20
Finance			
NFCL	15th	22/02/2008	50
AFCL	14th	31/01/2008	20
UFCL	13th	07/11/2007	25
Insurance			
AICL	12th	07/02/2008	-
EICL	13th	05/06/2008	12.5

Source: Annual Report of SEBON

<u>Based on Table 4.1</u>

The table relates generally to the year of sanctioning the bonus share by corporate board and concerned authorities. The Table covers the bonus share issued by the sample corporate firms that has issued bonus share at least once during study period.

For analyzing the data, we select 21 corporate firms who have issued bonus share in the Period of 2003/2004 to 2007/2008. Out of them few corporate firms have issued both stock and cash dividends. During F/Y 2003/2004 to 2007/2008 the range of bonus share declaration is 10% to 60%. Annapurna Finance Limited issued highest bonus ratio i.e. 60%. Whereas in the F/Y 2003/2004 to 2007/2008 Nepal Industrial and Commercial Bank, Alliance Insurance Co Ltd., National Finance, issued lowest bonus ratio i.e. 10%. Studying the 5 fiscal year data from 2003/2004 to 2007/2008 it is known that Himalayan Bank from banking sector is issuing bonus share regularly though the bonus ratio is decreased, in the same way, Annapurna Finance Company & National Finance among finance company are issuing bonus share frequently While, other corporate firms are also issuing bonus share as per their need because issue of bonus share is nothing more than a recapitalization of the company & the bonus ratio is also moderate.

4.2.1 Comparison of Stock Prices Before and After Bonus Share Issue

The impact on stock price after issue of bonus share is analyzed here. Generally, after bonus share announcement Market Price decreases, from the table below we can tabulate before bonus share announcement price and after bonus share announcement price and their percentage differences. Before price is the closing market price one to two month before the ex-dividend date and after price is the closing market price one to three month after ex-dividend date (here ex-dividend date is taken the date of AGM because some of the firms ex-date were not available). Since the data is taken from the secondary sources so we have to depend on them, while taking data sometime it happened that the stock were not traded for long time of those corporate firm which we are taking sample data.

Table 4.2

Stock Prices Before and After Bonus Share Issue and Their Percentage Difference:

	Before Price	**After Price**	**Difference in Price**
Year(2003/2004)			
Commercial Banks			
HBL	860	870	1.16
EBL	-	-	-
NIC	-	-	-
Finance Company			
NFCL	195	150	-23.08
AFCL	-	-	-
UFCL	125	105	-16.00
Insurance			
AICL	112	103	-8.04
EICL	650	630	-3.08
Year(2004/2005)			
Commercial Banks			
HBL	1110	1005	-9.46
EBL	-	-	-
NIC	-	-	-
Finance Company			
NFCL	295	250	-15.25
AFCL	512	463	-9.57
UFCL			
Insurance			
AICL	150	132	-12.00
EICL	301	295	-1.99
Year(2005/2006)			
Commercial Banks			
HBL	1110	1030	-7.21
EBL	970	879	-9.38
NIC	450	400	-11.11

Finance Company			
NFCL	290	250	-13.79
AFCL	537	400	-25.51
UFCL	-	-	-
Insurance			
AICL	-	-	-
EICL	301	295	-1.99
Year(2006/2007)			
Commercial Banks			
HBL	1210	1000	-17.36
EBL	1550	1665	7.42
NIC	500	651	30.20
Finance Company			
NFCL	300	300	0.00
AFCL	501	555	10.78
UFCL	131	130	-0.76
Insurance			
AICL	-	-	-
EICL	-	-	-
Year(2007/2008)			
Commercial Banks			
HBL	2728	1550	-43.18
EBL	2950	2640	-10.51
NIC	1259	1345	6.83
Finance Company			
NFCL	520	1075	106.73
AFCL	610	1107	81.48
UFCL	231	230	-0.43
Insurance			
AICL	-	-	-
EICL	399	390	-2.26

Source: Annual Report of SEBON and Trading Report of NEPSE

Note: % difference is calculated as = $\frac{After\ Price - Theoretical\ Price}{Theoretical\ Price}$ *x 100%*

Table 4.2 shows that the stock price fluctuates when bonus share is issued by the corporate firms, in most of the cases the stock price decreases but sometimes it increases. In this context theoretical assumption proves to be correct as the market price of stock decreases after issue of bonus share. Whenever a shareholder receives a bonus share, a rationale shareholder sells the bonus share because he knows that in almost cases share prices will decrease after issue of bonus share. The table also reveals that difference in percentage of share price before and after bonus share issue. The largest share price decrease after announcement of bonus issue is of HBL by Rs.1178/- with percentage difference of -43.18% and lowest decrease price of stock is Everest Insurance Co. Ltd. ie.Rs.6 and the percentage difference is -1.99%.

From the above table it is concluded that the price of stock fluctuates after the issue of bonus share, either it increases or decreases but fluctuated price of the stock is not equal to the bonus ratio because issue of bonus share has signaling effect in the stock price. If the corporate firm needs an additional equity capital to meet the legal requirement firm can issue bonus share as the issuance of bonus share increases the firm's equity capital.

4.2.2 Comparison of Theoretical Price and Actual Market Price after Bonus Share issue

To find the impact of bonus share issue on Market Price of share, it is necessary to calculate the Theoretical Market Price. The Market Price after ex-dividend date is compared with Theoretical Market Price to measure the effects. This comparison results the firms to measure the impact of bonus share issue on Market Price of share, positive change in share price means share price after bonus share issue are higher than Theoretical Market Price which are fine indicator for shareholders and corporate firms, it means they have positive signalling effect. Negative change means share price after bonus share issue are lower than the Theoretical Price.

Table - 4.3

Calculation of Theoretical Market price of Stock After Bonus Share Issue.

(Ex-Dividend Date)

	Before Price	**CDPS**	**Bonus Ratio**	**Theoretical Price**
Year(2003/2004)				
Commercial Banks				
HBL	860	0	20.00	716.67
EBL	-	-	-	-
NIC	-	-	-	-
Finance Company				
NFCL	195	0	20.00	162.50
AFCL	-	-	-	-
UFCL	125	5	20.00	100.00
Insurance				
AICL	112	0	10.00	101.82
EICL	650	0	100.00	325.00
Year(2004/2005)				
Commercial Banks				
HBL	1110	0	20.00	925.00
EBL	-	-	-	-
NIC	-	-	-	-
Finance Company				0.00
NFCL	295	0	20.00	245.83
AFCL	512	463	50.00	32.67
UFCL	-	-	-	-
Insurance				
AICL	150	0	10.00	136.36
EICL	301	0	10.00	273.64
Year(2005/2006)				
Commercial Banks				
HBL	1110	11.5	20.00	915.42
EBL	970	0	20.00	808.33
NIC	450	10	20.00	366.67

	Before Price	CDPS	Bonus Ratio	Theoretical Price
Finance Company				
NFCL	290	0	10.00	263.64
AFCL	537	3.158	60.00	333.65
UFCL	-	-	-	-
Insurance				
AICL				
EICL	301	0	50.00	200.67
Year(2006/2007)				
Commercial Banks				
HBL	1210	30	5.00	1123.81
EBL	1550	25	30.00	1173.08
NIC	500	0	20.00	416.67
Finance Company				0.00
NFCL	300	0.53	10.00	272.25
AFCL	501	0.53	10.00	454.97
UFCL	131	10	0.00	121.00
				0.00
Insurance				
AICL	-	-	-	-
EICL	-	-	-	-
Year(2007/2008)				
Commercial Banks				
HBL	2728	15	15.00	2359.13
EBL	2950	10	30.00	2261.54
NIC	1259	1.05	20.00	1048.29
Finance Company				0.00
NFCL	520	5	50.00	343.33
AFCL	610	1.05	20.00	507.46
UFCL	231	11.84	25.00	175.33
Insurance				
AICL	-	-	-	-
EICL	399	0	12.50	354.67

Source: Annual Report of SEBON and Trading Report of NEPSE

$$\text{Theoretical price} = \frac{Before\,\mathrm{Pr}\,ice - CDPS}{1 + BonusRatio}$$

After tabulating the data in 4.3, 21 sample of corporate firms are taken among them 11 firms issued both cash & stock dividend while 10 issued only stock divided within the fiscal year 2003/2004 to 2007/2008. Throughout five fiscal year from 2003/2004 to 2007/2008 HBL has the highest theoretical price in the F/Y 22007/2008i.e. Rs.2359/- and UFCL and AICL has the lowest theoretical price in the F/Y 2003/2004 i.e. Rs.102/- For the fiscal year 2007/2008 among the sample corporate firms five firms have given both cash & stock dividend.

Table - 4.4

Comparison between Theoretical Price and Actual Market Price after Bonus Share Issue.

	After Price	**Theoretical Price**	**Percentage Change**
Year(2003/2004)			
Commercial Banks			
HBL	870	716.67	21.39
EBL	-	-	-
NIC	-	-	-
Finance Company			
NFCL	150	162.5	-7.69
AFCL	-	-	-
UFCL	105	100	5.00
Insurance			
AICL	103	101.82	1.16
EICL	630	325	93.85
Year(2004/2005)			
Commercial Banks			
HBL	1005	925	8.65
EBL	-	-	-
NIC	-	-	-
Finance Company		0	
NFCL	250	245.83	1.70
AFCL	463	32.67	1317.20
UFCL	-	-	-
Insurance			
AICL	132	136.36	-3.20
EICL	295	273.64	7.81

Year(2005/2006)			
	After Price	Theoretical Price	Percentage Change
Commercial Banks			
HBL	1030	915.42	12.52
EBL	879	808.33	8.74
NIC	400	366.67	9.09
Finance Company			
NFCL	250	263.64	-5.17
Finance Company			
Year(2005/2006)			
AFCL	400	333.65	19.89
UFCL	-	-	-
Insurance			
AICL	-	-	-
EICL	295	200.67	47.01
Year(2006/2007)			
Commercial Banks			
HBL	1000	1123.81	-11.02
EBL	1665	1173.08	41.93
NIC	651	416.67	56.24
Finance Company			
NFCL	300	272.25	10.19
AFCL	555	454.97	21.99
UFCL	130	121	7.44
Insurance		0	
AICL	-	-	-
EICL	-	-	-
Year(2007/2008)			
Commercial Banks			
HBL	1550	2359.13	-34.30
EBL	2640	2261.54	16.73
NIC	1345	1048.29	28.30

	After Price	**Theoretical Price**	**Percentage Change**
Finance Company			
NFCL	1075	343.33	213.11
AFCL	1107	507.46	118.15
UFCL	230	175.33	31.18
Insurance			
AICL	-	-	-
EICL	390	354.67	9.96

Source: Annual Report of SEBON and Trading Report of NEPSE

NOTE: % Change is calculated as = $\frac{After\ \mathrm{Pr}\,ice - Theoretical\ \mathrm{Pr}\,ice}{Theoretical\ \mathrm{Pr}\,ice}$ X 100%

After comparing the Theoretical Price and Actual Market Price after Bonus Share issue, the Table shows the difference in percentage between Actual Market Price and Theoretical Price. The Table 4.4 includes the calculated value of stock price after issue of stock dividend of Actual Market Price & Theoretical Price. In the F/Y 2003/2004, HBL after issue of bonus share, the stock price is Rs870/- but the Theoretical Market Price is Rs.717/- and their difference in % is positive i.e. 21.4%. The maximum difference between Theoretical Price and Actual Market Price is 129.61%, which is of National finance. During the study period the percentage change in share price of commercial banks is -2.54 % to 30.81%. The after price of share is greater than the theoretical price in most of the cases. In the year 2006/2007 and 2007/2008 the actual price is less than the theoretical price of the share. In case of the other sample firms the actual price is greater than the theoretical price.

Table 4.5

Bonus Share announcement in F/Y 2007/2008

Name of the Corporate Firm	**Bonus Ratio %**
Commercial Banks	
Himalyan Bank Ltd.	15
Everest Bank Ltd	30
Nepal Industrial & Commercial Bank Ltd	20
NABIL Bank Ltd	40
Nepal Investment Bank Ltd	25
Standard Chartered Bank Ltd	50
Nepal SBI Bank Ltd	35
Kumari Bank Ltd	20
Development Credit Bank Ltd	12
Siddhartha Bank Ltd	10
Development Bank	
Chimike Development Bank Ltd	73.68
Nirdhan Utthan Bank Ltd	10
Bagheshwori Development Bank Ltd	10
Deproxe Development Bank Ltd	30
Bhrikuti Development Bank Ltd	20
Siddhartha Development Bank Ltd	15
Narayani Development Bank Ltd	25
Swalamban Development Bank Ltd	25

Finance Companies	
Nepal Finance Company Ltd	50
NIDC Capital Markets Ltd	35
National Finance Co. Ltd.	10
Nepal Housing and Merchant Finance Ltd.	35
Annapurna Finance Co. Ltd.	20
Narayani Finance Co. Ltd	35
Janaki Finance Co. Ltd.	25
Lalitpur Finance Co. Ltd	50
Kathmandu Finance Co. Ltd	15
Nawa Durga Co. Ltd	15
Mahalaxmi Finance Co. Ltd	21.21
Shree Finance & Investment Co. Ltd	20
Nagarik Lagani Kosh	33.33
Universal Finance Co. Ltd	20
Goodwill Finance Co. Ltd	10
Paschimanchal Finance Ltd	29.66
Lumbini Finance & Leasing Co. Ltd	50
Siddhartha Finance Co. Ltd	30
Central Finance Co. Ltd	15.5
United Finance Co. Ltd	25
Premium Finance Co. Ltd	15
Standard Finance Co. Ltd	10
World Merchant Banking & Finance Co. Ltd	10
Birgunj Finance Co. Ltd	20
Capital Merchant Banking & Finance Co. Ltd	15
Royal Merchant Banking & Finance Co. Ltd	10
Guheshowri Merchant Banking & Finance Co. Ltd	12
Bhajuratna Finance & Saving Ltd	10

Insurance Companies	
Himalayan General Insurance Co. Ltd.	110
United Insurance Co. Ltd.	20
Premier Insurance Co. Nepal Ltd.	100
Everest Insurance Co. Ltd.	12.5
Other Companies	
Bishal Bazar Co. Ltd.	80

Source: Annual Report of SEBON

Out of 112 corporate firms holding AGM in the Fiscal Year 2007/2008, 16 corporate firm have declared cash dividend, 25 declared both cash and stock dividend and 28 firms issued only bonus shares, the range of the stock dividend declaration is 10 to 110 percent. In this year corporate firms issuing stock dividend were 10 commercial bank, 8 development bank, 28 finance companies, 4 insurance companies & 1 other company. The trend of issuing stock dividend for the last year from the fiscal year 2003/2004 to 2007/2008 is shown below with graph:

Table 4.6

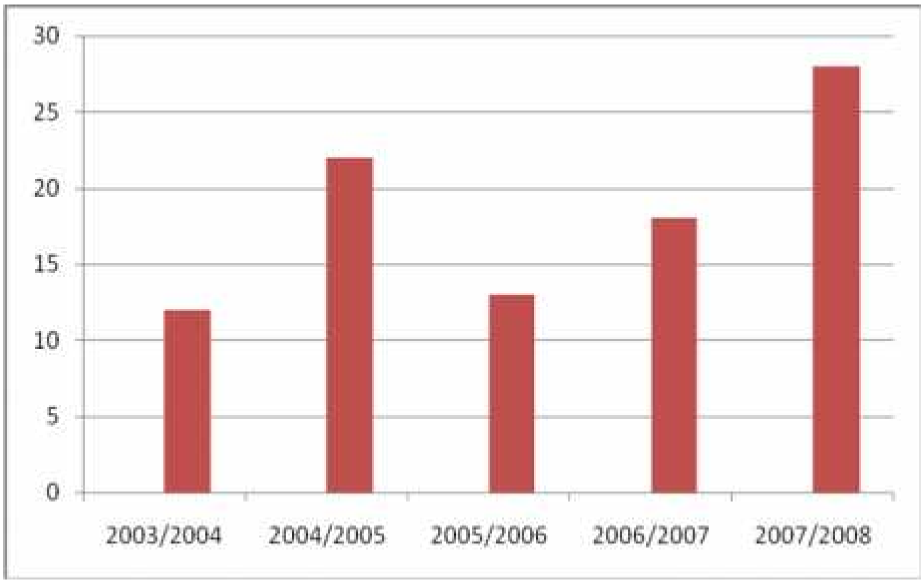
Trend of stock dividend

No Fiscal Year	No of firms issuing bonus share
2003/2004	12
2004/2005	22
2005/2006	13
2006/2007	18
2007/2008	28

Source: Annual Report of SEBON

Figure 4.1

Trend of stock dividend



The above table and the figure show the no of corporate firms issuing the bonus share in the fiscal year 2003/2004 to 2007/2008. The no of firms issuing the bonus share ranges from 12 to 28. In the year 2003/2004 12 firms issued bonus share and 28 firms issued bonus shares in the year 2007/2008.

4.2.3 Analysis of Minimum Stock Dividend Rate

Table 4.7

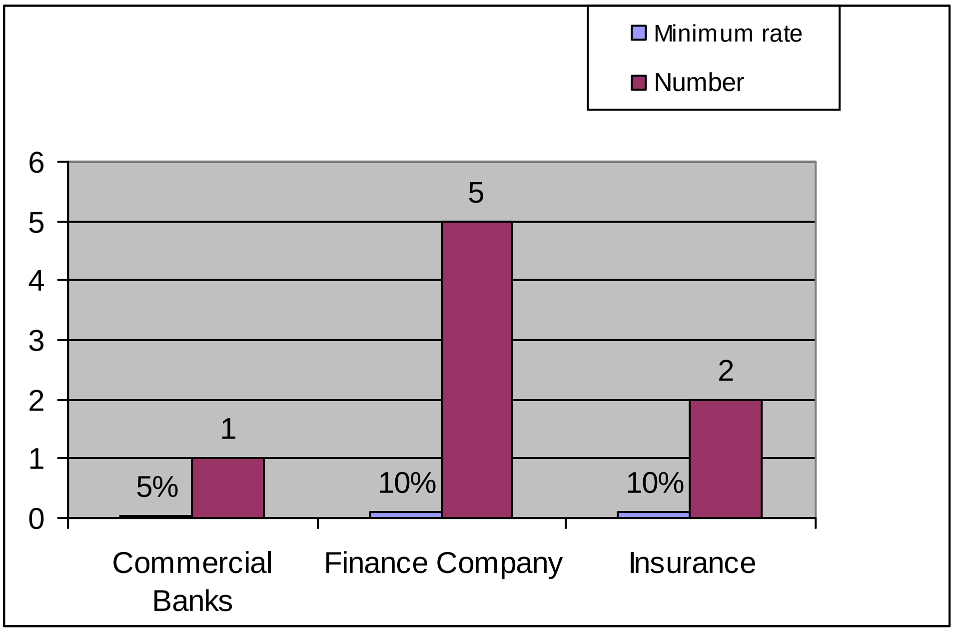
Analysis of stock dividend rate

Financial Institution	Minimum Rate	No
Commercial Banks	5%	1
Finance Company	10%	5
Insurance	10%	2

Source: Annual Report of SEBON

Figure 4.2

Analysis of Minimum Stock Dividend Rate



In last Five – years, minimum rate of issuing Bonus Share is 5% in Commercial Bank and 10% in other financial institution. In this period, only one bank issued 5% bonus share, 7 corporate firm issued 10% stock dividend Rate, with 5 Finance Companies and 2.

4.2.4 Analysis of Maximum Stock Dividend (Bonus Share) Rate

The Maximum Stock dividend Rate issued by the Company in the Five-Year period was 60%. By AFCL in the fiscal year 2005/2006.

Table 4.8

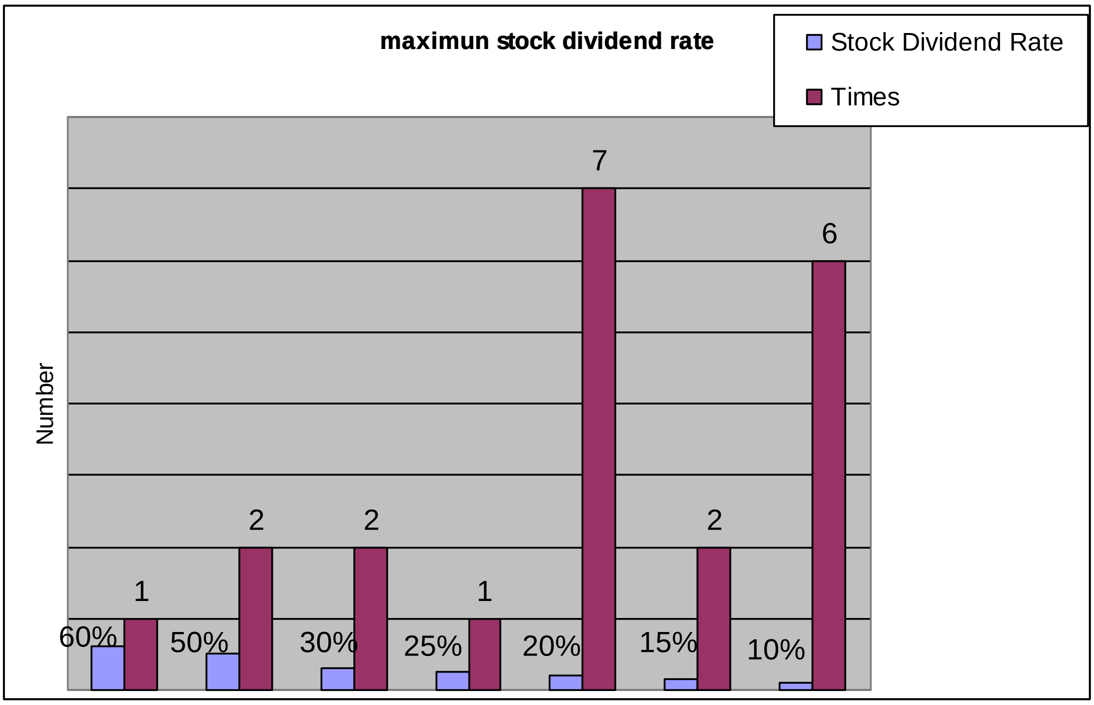
Analysis of Maximum Stock Dividend Rate:

Stock Dividend Rate	Times
60%	1
50%	2
30%	2
25%	1
20%	7
15%	2
10%	6

Source: Annual Report of SEBON

Figure 4.3

Analysis of Maximum Stock Dividend Rate



From the Table 4.8 the Nepalese Corporate Firms prefer 20% dividend rate in issuing stock dividend in Five – Year periods. They issued 7 times 20% stock dividend. After 20% they issued 10% stock dividend for 6 times. The rate of stock dividend of 15%, 30%, and 50% was issued for 3 times. Similarly 60% stock dividend was declared for 1 time only. From the above table it is revealed that 20% is the most popular stock dividend rate in Nepal.

Table 4.9

Share Prices of Three days Transactions on NEPSE before and after ex-dividend date of sample commercial banks

Firms	First Transactions	Second Transactions	Third Transactions	Ex Dividend Date	First Transactions	Second Transactions	Third Transactions
HBL	2095	2180	2220		1985	1995	1900
NIC	1600	1630	1650		1759	1761	1764
EBL	2820	2775	2830		2774	2718	2664

Source: Annual Report of SEBON and Trading Report of NEPSE

Above Table 4.9 reveals the price difference of commercial banks between before and after Ex-dividend date. Among the sample corporate firms we mention only share price of commercial banks because commercial banks are actively trading on NEPSE compared to other corporate films.

4.3 Testing of Hypothesis

The test of Hypothesis is a process of testing of significance regarding the parameter of the population on the basis of sample drawn from the population. In testing Hypothesis, we examine on the basis of statistics computed from sample drawn whether the sample drawn belongs to the parent population with certain specified characteristics. The computed value of statistic may differ from hypothetical value of the parameter due to the Sampling fluctuation; the test of hypothesis discloses the fact whether the difference between the computed statistic and hypothetical parameter is significant.

Null Hypothesis H_0: $\mu x = \mu y$, that is Actual Market Price after bonus share issue and Theoretical Price after bonus share issue are same. In other words, there is no significant difference in between Theoretical Price and Actual Market Price after bonus share issue.

Alternative Hypothesis H_1: $\mu x \neq \mu y$, which is Actual Market Price after bonus share issue is not equal to the Theoretical Market Price. In other words, there is significance difference between Theoretical Market Price and Actual Market Price after bonus share issue. (Two tail- test).

Based on Annex I

Decision: Since Calculated value of $|t| = 14.32$, is greater than the tabulated value of 't' = 2.021. Since $|t|$ is greater than't' alternative hypothesis is accepted which means there is significance difference between Actual Market Price and Theoretical Market Price after issue of stock dividend.

Table – 4.10

Frequency Distribution of Bonus issue Ratio in Sample Corporate Firms

(2003/2007 to 2007/2008)

Ratio of Bonus to issue outstanding equity	No. of Bonus Share issue	Percentage of Total %
1:1.67	1	4.76
1:2	2	9.52
1:3.33	2	9.52
1:4	1	4.76
1:5	7	33.33
1:6.67	2	9.52
1:10	6	28.57
Total	21	100%

Source: Financial Statement of Listed Companies, NEPSE

Table 4.10 presents the frequency distribution of bonus share issue according to certain specific bonus ratios. The Table reveals that Nepalese Corporate Firms followed a wide variety of bonus share ratio ranging from 1:1.67 to 1:10. It was found that out of many bonus ratios in practice few ratios were more popular among the corporate firms. During the period the largest portion (33.33%) of bonus share issue was in the ratio of 1:5 followed by 1:10 accounted for 28.57%, ratio 1:2, 1:1.33 and 1:1.67 accounted for 9.52%. The ratio 1:1.67 and 1:4 was used for 4.76 %.

4.3.1 Regularity and Frequency of Bonus Share issue

Table 4.12 gives a frequency distribution of Corporate Firms according to number of times Bonus Share are issued by the same Corporate Firm during the period under the study.

Table 4.11

Distribution of Corporate Firm According to Frequency of Bonus issue made by the same Corporate Firm during the period 2003/2004 to 2007/2008

No. Of Bonus issue by Each Corporate Firm	No. Of Corporate Firms
1	4
2	1
3	-
4	2
5	1
Total	8

Source: Financial Statements of Listed Company, NEPSE

Five Year period HBL was the only corporate firm, which made five-time bonus issue, AFCL, and NFCL issued four times over the period and EBL and NIC issued bonus shares two times. Where asAICL, UICL and EICL each made only one bonus share issue over the study period.

However there seemed to have been no regular and consistent policy regarding bonus issue in terms of bonus ratios and time interval between one bonus issue and another. The popular Bonus Ratio range from 10% to 60% and time interval remains from 1 to 5 years.

4.4 Presentation and Analysis of Primary Data

Primary data are collected from Shareholders' survey by using questionnaires. The main tool that is used in survey research is questionnaire. A questionnaire is a formal list of questions designed to gather responses from respondents on a given topic. Thus, a questionnaire is an efficient data collecting mechanism when the research is known exactly what is required and how to measure the variables of interest (Wolf & Pant, 1999: 144) the questionnaire survey method is used to analyze the Bonus Share issue practices of Corporate Firms in Nepal. Samples are taken from different sectors such as Banking, Financial, Insurance & Hotels Companies. The result is analyzed carefully so that it could lead to real problems and prospects of Stock market in Nepal. In this research study, 30 aggressive general investors are taken for the Shareholders survey. Those Shareholders taken and serious in investing Stock and buy Stock for active trading.

4.4.1 Questionnaire Survey based on Annex III

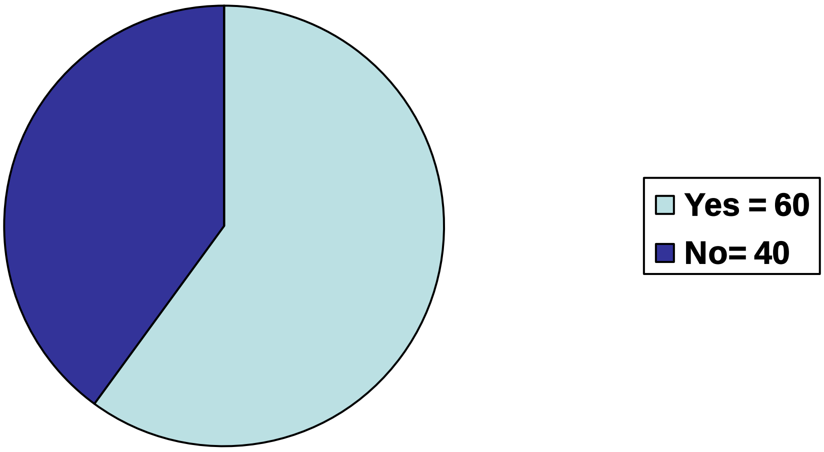
Do shareholders hold the stock and traded in Nepal Stock exchange?

	Number	**Percentage (%)**
Yes	18	60
No	12	40

Source: Annex II, Que No: 1

Figure4.4

Trading share in Nepal Stock Market



Regarding this question among the respondents 60% respondents hold the shares and they traded their share in NEPSE, while rest of the respondents holds their share without trading.

What may be the reason to pay bonus share & what you want to receive as a dividend?

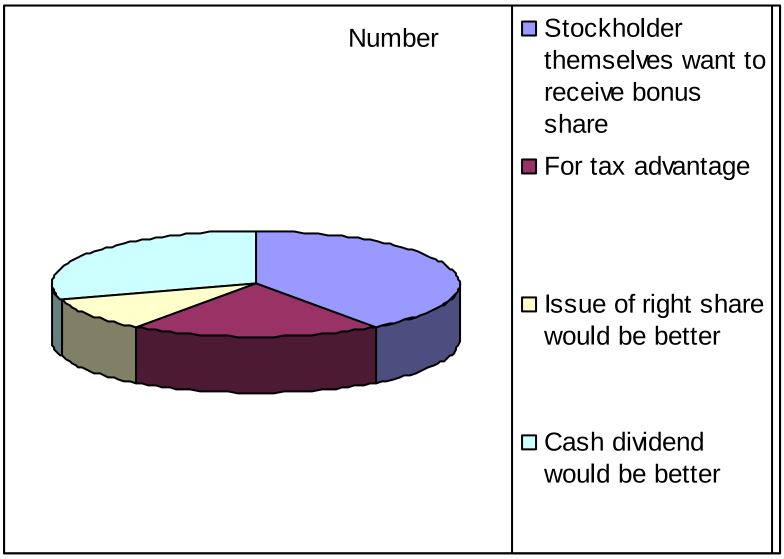
Table 4.12

Reasons for paying bonus share

Reasons	**Number**	**Percentage (%)**
Stockholder themselves want to receive bonus share	12	40
For tax advantage	6	20
Issue of right share would be better	3	10
Cash dividend would be better	9	30

Figure 4.5

Reasons for paying bonus share



Source: Annex II, Que No: 2

Regarding the question 40% i.e. 12 of the respondents are of the opinion that shareholders themselves want to receive bonus share to fulfil the legal requirement and to maintain existing control position, about 20% i.e. 6 respondents told that firm pays the bonus share to provide tax advantage to the shareholders and to attract the probable investors in their firm. 10% i.e. 3 of the respondents want right share and remaining 30% i.e. 9 respondents want to receive cash dividend instead of bonus share.

Major motive for issuing bonus share

Table 4.12

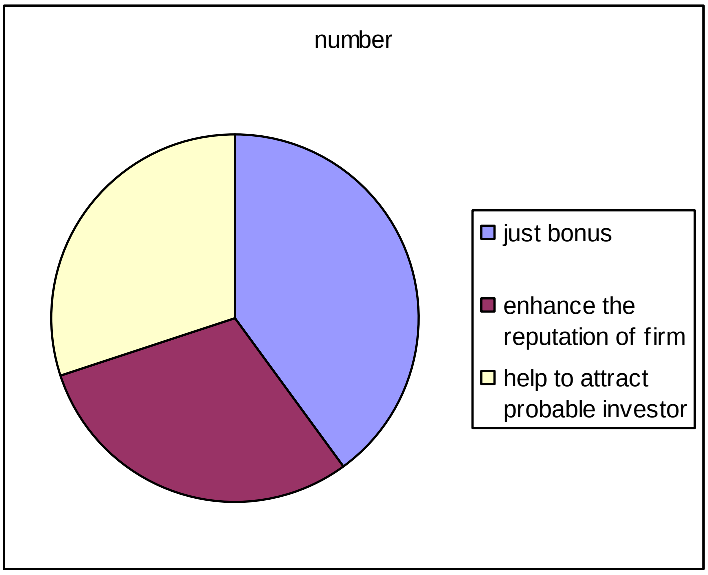
Motive for issuing bonus share

Motive	**Number**	**Percentage (%)**
Just Bonus Share	12	40
Enhance the reputation of corporate firms	9	30
Help to attract probable Investor	9	30

Source: Annex II, Que No: 3

Figure 4.6

Motive for issuing bonus share



In this research study, from questionnaire survey, 40% of the respondents expects to receive bonus share, 30% respondents respond that issuance of bonus share enhance the firms reputation in the market, 30% opines that issue of bonus share attracts the probable investors for investment in the firm.

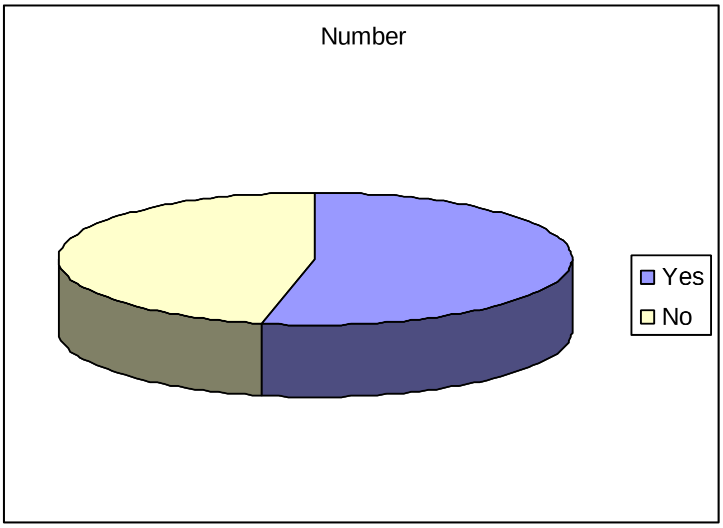
Shall firm need to pay bonus share as a residual decision in Nepalese enterprises?

	Number	Percentage (%)
Yes	16	53.33
No	14	46.67

Source: Annex II, Que No: 4

Figure 4.7

Decision for pay or not to pay bonus share



From the shareholders survey out of 30 respondents, 16 respondents agreed this statement stating that through bonus share they can maintain their holding position, followed by 14 who disagreed on this

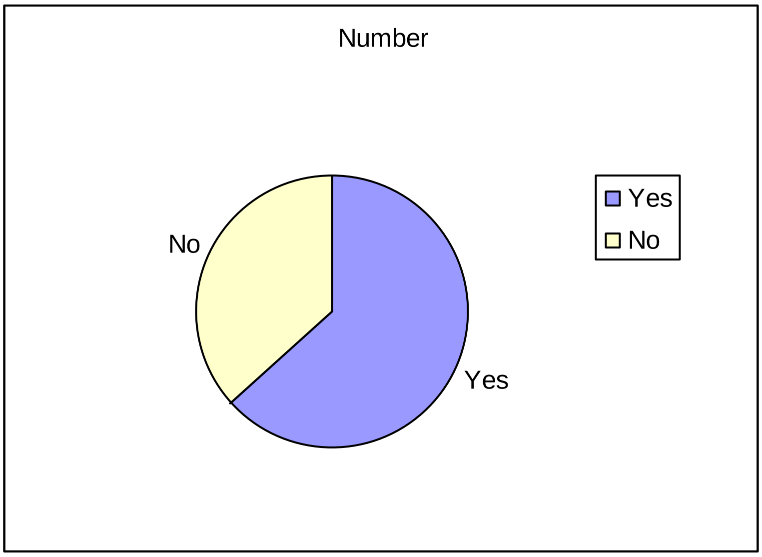
Does issue of bonus share helps to increase market price of share?

	Number	Percentage (%)
Yes	19	63.33
No	11	36.67

Source: Annex II, Que No: 5

Figure 4.8

Bonus share increase the MPS or not



Regarding this question, 40% respondents told that firm's announcement of bonus share help to increase market price of share. 30% told that issue of bonus share decreases the market price of share, while rests of them told that issue of bonus share doesn't affect the market price of share.

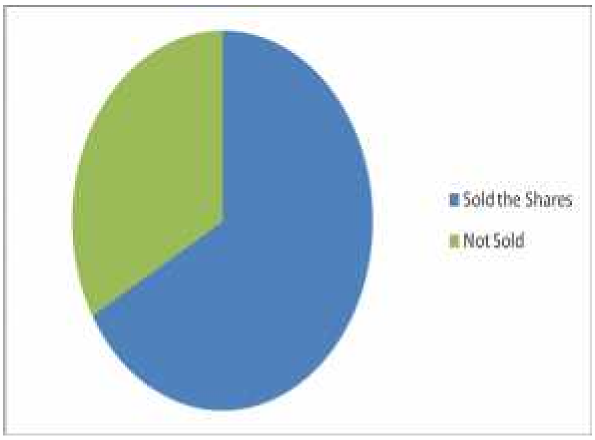
Frequency of Share Trading

	Number	**Percentage (%)**
Sold the Shares	20	66.67
Not Sold	10	33.33

Source: Annex II, Que No: 6

Figure 4.9

Frequency of Share Trading



Out of 30 respondents, 20 shareholders have sold their shares in share market and 10 haven't traded their shares.

Specify the reasons for selling stock

Among the shareholders who have sold their stock, 26.67% (5 respondents) expressed they sold their stock because no: of bonus share was not up to their expectation 13.33%(3 respondents) sold their stock to improve their rise of portfolio.40%(8 respondents) expressed they sold their share because stock price will decrease recently after issue of bonus share followed by 20%(4 respondents) expressed market price of share reached maximum at the time they sold their shares.

Table 4.14

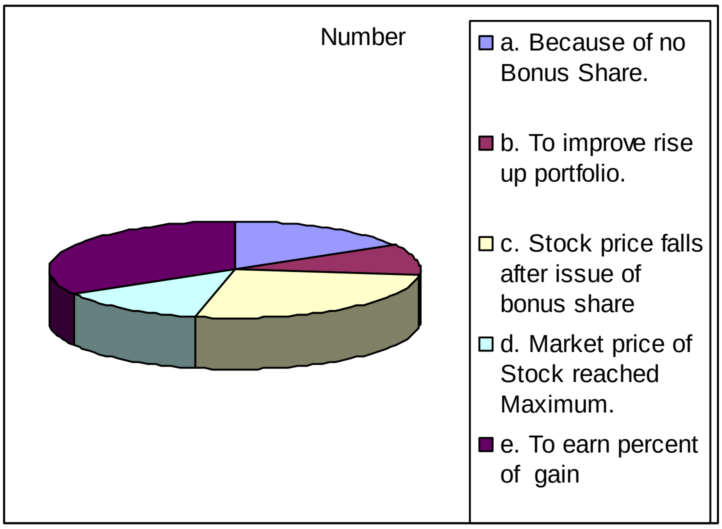
Causes of Selling Stock by Shareholders

S.N.	Causes of Selling Stock	Number	%
a.	Because of no Bonus Share.	5	16.67
b.	To improve rise up portfolio.	3	10
c.	Stock price falls after issue of bonus share	8	26.67
d.	Market price of Stock reached Maximum.	4	13.33
e.	To earn percent of gain	10	33.33

Source: Annex II, Que No: 7

Figure 4.10

Causes of Selling Stock by Shareholders



Based on Table 4.14

The above table 4.14 revealed that 10% i.e.3 investors want to improve rise up portfolio and 13.33 % i.e.4 investor sold their share because stock price they thought was maximum at the time they traded, 16.67% i.e.5 of investors sold their stock because of just bonus share, 26.67% i.e.8 investors sold their stock due to fall in stock price after bonus issue and 33.33% i.e. investor sells their share to earn percentage of gain From the investor's survey, we can conclude that investor wants to improve rise up portfolio because investor want to diversify their risk and return, as investing in only one firm's security is more riskier than investing in more than one corporate firms securities therefore, shareholders want to diversify their risk, they want to maximize their return and minimize their risk in security. If the shareholders invest in only one corporate firm's share, in the future if the share price fall then shareholder has to suffer loss so, shareholders does not want to decrease their share price

Specify the reason for holding stock

Among the 10 shareholders who did not trade their share in stock market 30%(3 respondents) hold their share for future financial security or they were not introduced to the stock market as they have invested it for their future, 15%(1 respondents) hold their share in expectation of cash dividend while, 30%(3 respondents) hold their share in expectation of bonus share followed by 25%(3 respondents) shareholders didn't sold their share in expectation of increase of stock price.

Table 4.15

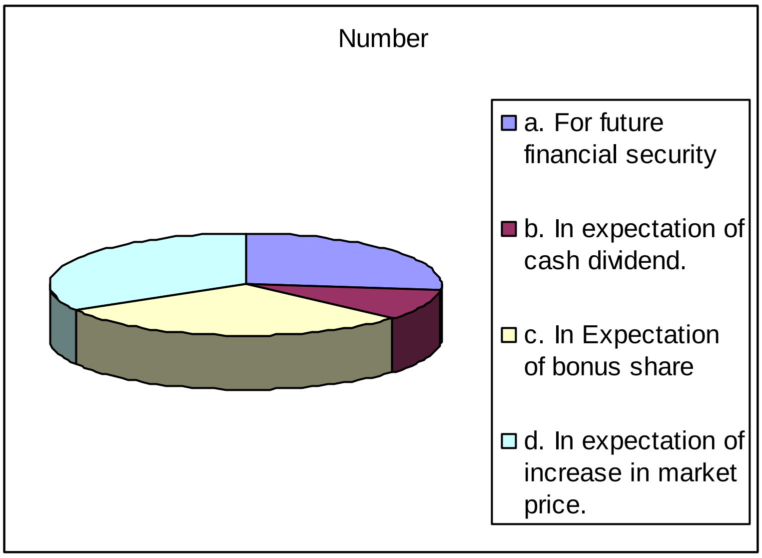
Causes of Holding Stock by Shareholders

S.N.	Causes of Holding Stock	Number	%
a.	For future financial security	8	26.67
b.	In expectation of cash dividend.	3	10
c.	In Expectation of bonus share	9	30
d.	In expectation of increase in market price.	10	33.33

Source: Annex II, Que No: 8

Figure 4.11

Causes of Holding Stock by Shareholders



Based on Table 4.15

Above Table 4.15 revealed that 10% i.e. 3 respondent hold their share in expectation of cash dividend , 33.33% i.e.10 respondent hold their share in expectation of increase in market price while26.67% i.e.8 respondent hold their shares for future financial security & 30% i.e.9s respondent hold their shares in expectation of bonus share in future average From this table we can conclude that respondent wants cash dividend as that can satisfy their present financial need, cash dividend helps to maintain their liquidity position strong compared to the stock dividend because stock dividend takes time to be converted into cash.

4.5 Major Findings of the Study

The Major Findings of the Study are as follows

<u>From Secondary Data:</u>

- The practice of bonus share issue is in increasing trend per year.
- Only 12 corporate firms issued bonus share but it reached to 28 firms issued for the fiscal year 2007/2008.
- The share price is decreased after the bonus share is issued in all cases but sometime share price is found increased in rare case.

- Corporate firm's especially financial sector in Nepal is practicing the issue of bonus share as a medium to provide dividend to the shareholders to increase the total capital fund.
- The popular dividend rate in Nepalese corporate firm is 20%, among the listed corporate firm in last 5 year they have issued for 7 times the stock dividend for shareholders.
- The minimum issuing stock dividend rate is 10% in Nepalese corporate firm in this 5 year among the listed corporate firm they have issued in this rate for 6 times.
- The maximum stock dividend rate is 60% & within these five years various corporate firms have issued stock dividend in this rate for 1 time.
- Manufacturing & Trading firms are not issuing bonus share in last 5 year due to high rate of inflation, political instability, low economic growth and the capital structure of the company.
- The actual market price & theoretical market price is not equal in the above table which means there is fluctuation in market price after issuance of bonus share.
- Most corporate firm's market price of share does not decrease as the same rate of stock dividend. This may be due to small knowledge of investors being immature market and the next reason could be investor's perception towards the corporate firm issuing bonus share is positive in stock market.
- During the study period, the maximum decrease in share price is of HBL in the fiscal year 2007/2008 by 43.18% i.e. Rs.1178/- and minimum decrease in share price is of NFCL by 0% 2006/2007.
- The maximum increase share price after bonus share issue is of NFCL in the fiscal year 2007/2008 Rs.555/- and with the maximum percentage changed of 106.73%.
- The hypothesis that actual market price after bonus share issue is not equal to the theoretical price which means there is significant difference between theoretical market price & actual market price.
- Most of the corporate firms are not maintaining their stock dividend rate regularly.
- Corporate firm's management have not been found considering the effects of bonus share distribution on dividend distribution in future as reflected by absence of systematic dividend planning practice before and after bonus share issue.

- Corporate firm are not practicing systematic policy regarding dividend distribution to the shareholders.
- Regarding the bonus issue, the corporate management has found not following consistent bonus ratio during the study period.
- It is revealed that the issue of stock dividend by various finance companies are higher than that of commercial banks.

From Primary Data:

- Investor’s perception towards those corporate firms which issues stock dividend is positive.
- From shareholders survey it is concluded that in the Nepalese stock market, people invest in stock for their future financial security for the sake of earning dividend at their retirement age.
- While analyzing the causes of holding stock, expectation of cash dividend ranked first, similarly in expectation of increased market price ranked second while shareholders hold their stock for their future financial security and in expectation of bonus share in future ranked third.
- 40% of the respondents expressed after bonus share issues shareholders wealth increases, while 30% expressed the shareholders wealth decreases and 30% expressed that there will be no change in their wealth.
- From the above study it is found that Nepalese stock market is still immature and the shareholders do not have depth knowledge about stock market. And few of the investors are playing in a speculative way in stock market.
- Shareholders are investing in stock because the rate of return is higher compared to any other saving account interest rate in any financial institutions.

CHAPTER - V

SUMMARY, CONCLUSION & RECOMMENDATION

5.1 Summary & Conclusion

It has been a recent phenomenon of corporate firms in Nepalese stock market issuing stock as a form of dividend provided to shareholders. Though, the Nepalese capital market has crossed more than a decade but still is an immature market, so the issue of stock dividend is a recent practice applied by the corporate market. The capital market is in developing stage; the investors are still unknown and are unable to interpret the information in right way.

The number of bonus share issued is in increasing trend in our capital market though it is infancy. Now, it has become an important and prevalent source for increasing the equity capital internally at a relatively lower cost of financing compared to external equity in Nepalese corporate practice. However, bonus share issue must be related to the objective of maximizing the welfare of its shareholders in terms of future dividend and capital gain. Besides raising additional equity capital by issuing bonus share must be justified by investment requirement in additional to the legal requirement.

The study duration is limited for five years from the fiscal year 2003/2004 to 2007/2008. Data are mainly collected from NEPSE, SEBON, Journals, Research papers & daily newspapers. During the study period 93 bonus shares were issued by various corporate firm and the samples were taken of 21 corporate firms. The date of announcement to shareholders about issuing of bonus share formally at an AGM of the corporate firm is taken as ex-dividend date. Various calculations has been done by using market price one month before ex-dividend date which is taken as before price and closing price after 3 month from ex-dividend date which is taken as after price.

The trend of issuing bonus share in last five has increased by the corporate firms. The major findings of this study are summarized below.

- The practice of issuing stock as a dividend in Nepalese capital market is in increasing trend. This may be due to the NRB's directives of raising the paid up capital of the corporate firms by the year 2070 Asadh.

- It is found that the stock price decreases after the announcement of stock dividend except in few cases. But the decreased price ratio does not match with the ratio of stock dividend rate.
- From the study it is found that the shareholders have great misconception about bonus share, the general investors think that they receive extra or additional share with same market value.
- The study also reveals that there is significant difference between actual market price & theoretical market price which shows that share price fluctuates with the issue of bonus share.
- Bonus share issuing corporate firms are taken as good firms by the shareholders and the investors perception towards those corporate firms are found positive. Probable investors are attracted by the announcement of stock dividend.
- The rumour about issuing of stock dividend by the management of the corporate firms raises the stock price in market before one month while the price decreases after few months of announcement.
- The stock price is increased till date of book close then afterwards the stock price in the market of bonus issuing firm decreases.
- Nepalese capital market is speculative-oriented; therefore it takes more consciously bonus share issue than cash dividend. Whatever the dividend policy of the company the immediate impact and a year later are significantly positive.
- The corporate firm issues bonus share without frequently cash dividend distribution, ultimately faces drastic fall in their share prices.
- The relation between bonus ratio and immediate price rise is positively correlated. High bonus ratio leads high magnitude of immediate price rise.
- It is found that market price of share increase in average 33.88% above the theoretical value after bonus share issue, which means impact of bonus share issue on market price is positive.
- Stock dividend is one of the major reasons of investing, selling and holding stocks of the shareholders.
- In overall corporate management have not been found considering effects of bonus share distribution on dividend distribution in future as reflected by absence of systematic dividend paying practice before and after bonus share issue. It is also found not universally true that corporate firms have issued bonus share not

necessarily with a view to increase the total dividend distribution as reflected by decrease in post bonus quantum of dividend in some corporate firms issuing the bonus Share.

- Corporate firms though are issuing stock dividend but the firms does not posses any systematic policy regarding stock dividend rate & distribution.
- Bonus share issue results in maximization of wealth only if there is increased dividend payment after bonus issue. This is positively issue only if increased capital raised internally through the bonus issue is desirable to that extent only that the corporate firms need additional financing for increase profitable investment.
- Bonus share is the recapitalization of the profit so when bonus share is issued, paid up capital of the firm increases while retained earnings decreases in the balance sheet.
- From the shareholders survey it is found that in the country like ours, common people invests in stock for their future financial security not in the way of making profit by selling them in secondary market.

5.2 Recommendation

Issue of bonus share itself doesn't have financial value; is recapitalization of profit & merely reshuffle of accounting heads. It is a transfer from retained earning from share capital & share premium. The allocation of profits between dividends and retentions is determined without regard to whether or not the retentions are to be capitalized immediately or after some years. Hence decisions about bonus issues have to be arrived at in the context of ex-post retention. It may have a favourable psychological effect on the shareholders.

This stage deals with only examining the bonus share issue practices of corporate firms in Nepal, of Nepalese corporate firms of 21 samples from the listed firm. Those firm that intents to pay dividend and also needs funds to finance its investment opportunities, in such condition issue of bonus share might be the best decision. The firm should use retained fund properly so that it can generate good return than the opportunity cost of shareholders. From the study period and brief analysis of the data the following recommendation have been made.

- Being immature stock market, the shareholders are not having enough knowledge of stock. It is found that shareholders are investing on primary market but only few of these are trading on secondary market. So, I recommend educating the shareholders about stock market. The corporate firms' must exercise educating the shareholders by publishing journals & these journals should be on the hands of shareholders at any cost.
- Legal rules and regulation must be amended which suits the corporate firm's requirements, to exercise control in bonus share issue practice and to protect shareholders interest.
- The issue of bonus share is practiced without any guideline by the Nepalese corporate firms. The regulation of issue of bonus share is also inadequate. There must be a procedure that the corporate firms require a prior approval of the concerned authority for issue of bonus share. That prior approval will protect the shareholders interest. The concerned authority must prepare a guideline regarding the dividend and each listed firm must abide by this guideline.
- The true objective behind the issue of bonus share must be disclosed for all stock holders. The information leakage before the actual announcement of bonus share must be prohibited and immediate action should be taken against those actions.
- Rumor and other misconceptions are obstacles for smooth growth of the stock market and increase the risk to the investors. Thus, the investor's right must be protected for smooth development of the stock market.
- For prospective development of capital market, investors must analyze the source of information and interpret the available data. Conscious investors with good knowledge about the capital market can only take the rational decision. But the general investor of our capital market is unable to get rational investment decision. Misconception and rumours about bonus share, leads them to take irrational decision. Thus, the concerned authorities must consider making aware to the investors regarding misconception held with bonus share and other influential factors. The awareness program can be done through publishing the matters frequently and should be available to all general investors it can be done through mass media and programs via seminars and workshops.
- Security Board should have mandated authority to observe the issue of bonus share before announced by the corporate firms. Bonus share issue must be subject

to sanction from Security Board. The main purpose of this control is to see that there is no malpractice by the shareholders.

- The statement that market value of share do not improve as a result of bonus share, it is not followed by increased dividends in the immediate future is accepted, so a corporate management should declare regular cash dividend with stock dividend.
- Consecutive bonus share issued by a corporate firm without cash dividend obviously invites a grave consequence for its share price. That may posses negative psychology to the investors. Therefore, regular cash dividend should be distributed to the shareholders.
- For the better performance and good psychological value to the investors, appropriate and convenient bonus ratio should be chosen.
- A firm should not declare bonus share without assessment of future consequences. If a firm does not have any profitable opportunities and less return then the shareholder doesn’t expects issue of bonus share. A firm must considered on effective, efficient and profitable utilization of additional equity raise via bonus share issue.
- A corporate firm must maintain its future policy after bonus share issue for true gain to the shareholders. Otherwise, the share price will fall ultimately and deteriorate the firm’s image.
- Management of the firm should prevent practicing of issuing bonus share to manipulate and as pretence for bidding of the price of the share beyond its true worth by market operators.
- I would like to suggest to the further researchers on the bonus share to observe recent behaviour and managerial aspect about bonus share issue.

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Annex I
Request letter

Dear respondents

The following questions have been put forwarded to you for your independent views and opinions about the Bonus Share. The responses and views obtained from your side will be kept confidential and will be used for this study purpose only. Please be kind and provide the rational information on the basis of their performances without hesitation. Thank You.

(Researcher)

Annex II

Pro-Forma of Structural Questionnaire.

A survey of shareholders' on Bonus Share issue practice of corporate firms & its impact on MPS:

Name (optional):-………………………………………….

1. Do you hold Stock? Are they traded in the Nepal Stock Exchange?

   (a) Yes:-………………………….. (b) No.:-……………………………

2. What may be the reason to pay bonus share & what you want to receive as a dividend?
   (Please make a tick –mark)
   (a) Shareholders themselves want to receive bonus share
   (b) Corporate firm pays bonus share for tax advantage & to attract probable investors
   (c) Issue of right share would be better
   (d) Cash dividend would be better

3. What do you think is the major motive for issuing bonus share?
   (a) As a shareholders I want bonus share
   (b) Issue of bonus share enhances the reputation of corporate firm
   (c) Issue of bonus share helps to attract the probable investors

4. Shall firm need to pay bonus share as a residual decision in Nepalese Enterprises?
   (a) Yes (b) No

5. Do you think that corporate firm's announcement of issuing bonus share will help to increase market price of a Share? (Please make a tick –marks)
   (a) Yes :……………….(b) No :………………(c) constant: ……………….

6. Have you sold the share in Stock Market? Please tick on choice.

   (a) Yes :………………………..(b) No: ……………………….

7. If you have, why did you sell the Stock?

(a) Because no: of bonus share was not up to the expectation

(b) To improve rise- up Portfolio.

(c) As stock price decreases after issue of bonus share.

(d) Market price of Stock reached maximum.

8. If you have not sold your stock then specify for holding the stock.

(a) For future financial security

(b) In expectation of additional cash dividend.

(c) In expectation of increased stock price

(d) In expectation of Bonus Share.

Annex: III

Calculation of Test statistics t

Firms	Actual Market Price (x)	Theoretical Market Price (y)	d=y-x	$d - \bar{d}$	$(\bar{d}-d)^2$
HBL	870	716.67	-153.33	-68.94	4752.72
EBL	-	-	-	-	-
NIC	-	-	-	-	-
NFCL	150	162.5	12.5	96.89	9387.67
AFCL	-	-	-	-	-
UFCL	105	100	-5	79.39	6302.77
AICL	103	101.82	-1.18	83.21	6923.90
EICL	630	325	-305	-220.61	48668.77
HBL	1005	925	-80	4.39	19.27
EBL	-	-	-	-	-
NIC	-	-	-	-	-
NFCL	250	245.83	-4.17	80.22	6435.25
AFCL	463	32.67	-430.33	-345.94	119674.48
UFCL	-	-	-	-	-
AICL	132	136.36	4.36	88.75	7876.56
EICL	295	273.64	-21.36	63.03	3972.78
HBL	1030	915.42	-114.58	-30.19	911.44
EBL	879	808.33	-70.67	13.72	188.24
NIC	400	366.67	-33.33	51.06	2607.12
NFCL	250	263.64	13.64	98.03	9609.88
AFCL	400	333.65	-66.35	18.04	325.44
UFCL	-	-	-	-	-
AICL	-	-	-	-	-
EICL	295	200.67	-94.33	-9.94	98.80
HBL	1000	1123.81	123.81	208.2	43347.24
EBL	1665	1173.08	-491.92	-407.53	166080.70
NIC	651	416.67	-234.33	-149.94	22482.00
NFCL	300	272.25	-27.75	56.64	3208.09
AFCL	555	454.97	-100.03	-15.64	244.61
UFCL	130	121	-9	75.39	5683.65
AICL	-	-	-	-	-
EICL	-	-	-	-	-
HBL	1550	2359.13	809.13	893.52	798377.99
EBL	2640	2261.54	-378.46	-294.07	86477.16
NIC	1345	1048.29	-296.71	-212.32	45079.78
NFCL	1075	343.33	-731.67	-647.28	418971.40
AFCL	1107	507.46	-599.54	-515.15	265379.52
UFCL	230	175.33	-54.67	29.72	883.28
AICL	-	-	-	-	-

EICL	390	354.67	-35.33	49.06	2406.88
			∑d= -3375.6		∑(d-d)^2 = 2164715.825

$$\bar{d} = \frac{\sum d}{n}$$

= $\frac{-3375.6}{40}$

= -84.39

And,

$$S_d = \sqrt{\frac{1}{n-1}\sum(d-\bar{d})^2}$$

$$= \sqrt{\frac{1}{40-1} * 2164715.83}$$

= 235.59

Test Statistic

$$t = \frac{\bar{d}}{\sqrt{\frac{S^2}{n}}}$$

= - 14.32

Thus, │ t│= 14.32

Degree of freedom (d.f.) = n -1, 40 - 1 = 39

Level of significance (α) =5%,

Critical value: the tabulated value of 't' at 5% level of significance for two- tailed test and for 20d.f. is 2.021