CHAPTER I

INTRODUCTION

1.1. Background of the Study

Dividend payout has been an issue of interest in financial literature. Academician and researchers have developed many theoretical models describing the factors that managers should consider when making dividend policy decisions. By dividend policy, we mean the payout policy that managers follow in deciding the size and pattern of cash distribution to shareholders over time. Dividend policy is one of the most important financial policies, not only form the viewpoint of the company, but also from that of the shareholders, the consumers, the workers, regulatory bodies and the Government. For a company, it is a pivotal policy around which other financial policies rotate. Value of the corporate securities depends to a great extent on dividend and, therefore, in deciding upon the financial structure of company, dividend has to be assigned due to consideration. Dividends are payments made by corporations to its shareholder members. It is the portion of corporate profits paid out to stockholders. When a corporation earns a profit or surplus, that money can be put to two uses: it can either be re-invested in the business (called retained earning), or it can be paid to the shareholders as a dividend. Many corporations retain a portion of their earnings and pay the remainder as a dividend.

All the business corporations are operated for profit. Less or more their objective is profit earning. Traditionally the only one objective of firm used to be profit maximization. But with past in time, the consumers became aware and consumers' groups and various interest groups emerged against the profit maximization objective of the firm exploiting the natural resources and consumers. Due to this various objectives of the firms such as sales maximization, wealth maximization etc is in practice now. Even firms have different objectives; they are not completely able to ignore the objective of earning profit. As profit is the backbone of firm which determines the position of the firm in the market and maximizes the wealth of the firm, manager should make a decision that how much portion of the profit to be shared to shareholders and how much portion to be kept for further investment.

A company's total net income (profit) can be divided into two parts: Dividend and Retained Earnings. In general while the firm is in profit, the firm gives return to its investors from the profit amount in the form of cash or stock or property on their stock investment which is known as dividend. In other words, the portion of the profit that distribute to the shareholders for making investment and bearing risk in the form of cash or stock or property is called dividend. Dividend here refers to the share of profit/ earning distributed to its common stockholders rather than preference shareholders. The percentage of earnings paid out in the form of cash dividend is known as dividend payout ratio. Most of the firms in Nepal have a practice of distributing the profit in the form of cash dividend. But, in the recent days some of financial institutions started to give the dividend in the form of stock dividend also. A firm has three alternatives regarding the payment of cash dividends:

- Distributing whole profit amount as a cash dividend
- Retain the whole profit amount for further investment
- Partial of profit distribute as cash dividend and remaining to keep as retention.

On the other hand, another portion of profit kept in the firm rather than distributing to its common stockholders for further investment is defined as a retained earning. Retained earning is the part of profit amount kept for the purpose of utilizing the profit oriented investment opportunities. Higher the retained earning, higher the chance of investment in profitable sectors. The percentage of profit retained in the firm for investment purpose is known as retention ratio. The sum of dividend payout ratio and retained earning ratio will be 100 %.

Once a company makes a profit, the board of directors must decide what to do with those profits. They could continue to retain the profits within the company, or they could pay out the profits to the owners of the firm in the form of dividends. Once a company decides to pay dividends, there should be established a somewhat permanent dividend policy, which would impact on investors and perceptions of the company in the financial markets providing information concerning the firm's performance. The choice of the appropriate dividend policy depends on the preferences of investors and potential investors as well as on the company's capital structure and its future plan. The board of directors holds a prominent position both

with regard to the company as well as shareholders. The board of directors must combine the three decisions pertaining to investment, financing and dividends simultaneously as these three decisions are interrelated. dividend policy decision influences the financing decision of the firm through retained earnings. Financing decision would relate to the amount of funds to be raised from external sources as the investment needs of a firm can be fulfilled by a combination of retained earnings and external financing. Therefore, higher the amount of retained earnings, given the investment needs, lower will be the need for external finance and vice-versa.

1.2 Dividend Policy

Dividend policies are the regulations and guidelines that companies develop and implement as the means of arranging to make dividend payments to shareholders. Establishing a specific dividend policy is to the advantage of both the company and the shareholder. In order to make sure the policy is workable, a company should develop a viable policy and then run this policy through a number of test scenarios in order to determine what impact the dividend policy would have on the operation of the business. In many cases, companies choose to explicitly state the provisions within the dividend policy. This is definitely to the advantage of the shareholder, as a well defined policy makes it much easier to project the amount of payout profits generated for the period under consideration and thus be able to determine the size of the dividends that will be issued. When the dividend policy is well defined and documented, it is easy for the shareholder to obtain a written copy and thus be fully informed as to how the policy works.

Dividend policy is one of the most important financial policies, not only form the viewpoint of the company, but also from that of the shareholders, the consumers, the workers, regulatory bodies and the Government. For a company, it is a pivotal policy around which other financial policies rotate. Value of the corporate securities depends to a great extent on dividend and, therefore, in deciding upon the financial structure of a company, dividend has to be assigned due consideration. In cases where the dividend policy is not specifically defined, investors often look at the history to spot any trends that emerged in the past. If the dividend payments have been more or less constant for the last several years, and there has been no loss in business volume, it is reasonable to assume the payments will still be in the same general range as before.

However, if the dividend history is more volatile, the shareholder may attempt to identify what factors led to the up and down movement of the dividends and determine if any of those factors are relevant to the current dividend period.

1.3 Commercial Banks

The name bank derives from the Italian word banco "desk/bench", used during the renaissance by Florentine bankers, who used to make their transactions above a desk covered by a green tablecloth. However, traces of banking activity can be found even in ancient times. In fact, the word traces its origins back to the Ancient Roman Empire, where moneylenders would set up their stalls in the middle of enclosed courtyards called macella on a long bench called a bancu, from which the words banco and bank are derived. As a moneychanger, the merchant at the bancu did not so much invest money as merely convert the foreign currency into the only legal tender in Rome- that of the Imperial Mint. A bank is a financial intermediary that accepts deposits and channels those deposits into lending activities. Banks are a fundamental component of the financial system, and are also active players in financial markets. The essential role of a bank is to connect those who have capital (such as investors or depositors), with those who seek capital (such as individuals wanting a loan, or businesses wanting to grow).

Banks which are established to accept deposits and grant loans to the industries, individuals and traders with a view point to earn profits are known as commercial banks. Commercial banks are established as the joint stock company. Establishment of commercial banks is to accept as deposit to the unused amount of one type of client and promoting to another type of client to use such amount as loan. It provides mid term, short term loan and long term long against the securities placed. Commercial banks are those banks, which perform all kinds of banking functions as accepting deposits, advancing credits, credit creation and agency functions etc. They provide short term credit, medium credits and long-term credits to trade and industries. They also operate off-balance sheet functions such as issuing guarantee, bonds letter of credit etc.

Commercial banks engage in processing of payments by way of telegraphic transfer, EFTPOS, internet banking, or other means, issuing bank drafts and bank cheque,

accepting money on term deposit , lending money by overdraft, installment loan, or other means, providing documentary and standby letter of credit, guarantees, performance bonds, securities underwriting commitments and other forms of off balance sheet exposures, safekeeping of documents and other items in safe deposit boxes, sale, distribution or brokerage, with or without advice, of insurance, unit trusts and similar financial products as a “financial supermarket” , cash management and treasury services , merchant banking and private equity financing , traditionally, large commercial banks also underwrite bonds, and make markets in currency, interest rates, and credit-related securities, but today large commercial banks usually have an investment bank arm that is involved in the mentioned activities.

To sum up, a bank is defined as a financial institution, which performs widest range of economic and financial functions of any business firms in the economy. The commercial bank is that financial institutions which collect scattered savings of the people and provide loan against proper securities for their productive purpose. Moreover they also provide technical help and suggestions, administrative suggestions, safekeeping of valuables, collections of bills, cheque and overdraft facilities to industries and commerce.

1.4 Brief Profile of Samples

In this study, due to time consistency and reliability of the data available, only seven companies are selected as sample among enlisted commercial banks of NEPSE. Following are the brief introduction of them

Nepal Investment Bank Ltd.

Nepal Investment Bank Limited, one of the A-category enlisted banks of NEPSE offers a wide range of services. Some of them are Trade finance, deposits, fund transfer, remittances, export credit, bills purchase, loans and advances, locker facilities, ATM with any branch banking 365 days banking etc. Nepal Investment Bank Limited, formerly Nepal Indosuez Bank Limited was established in 1986 as a joint venture between Nepalese and French partners. The French partner holding 50% of the capital of NIBL was credit Agricole Indosuez, a subsidiary of one of the largest banking group in the world. On April 2002, Agricole Indosuez withdrew its 50% share from NIBL and a group of companies consisting of Bankers, Professionals,

Industrialists and Businessman has acquired those 50% of shares. The name of the bank has changed as Nepal Investment Bank Limited on approval of its annual general meeting. 50%, 15%, 15% and 20% of the capital is held by a group of companies , Rashtriya Banijya Bank, Rashtriya Beema Sansthan and general public respectively.

Everest Bank Limited

Everest Bank Ltd. is a joint venture bank with Punjab national bank of India was Established in 18 th Oct 1994. This bank is established with 50 % of the shares are owned by the local promoters 20% by our joint venture partner Punjab National Bank India and 30% of the shares are owned by the general .It has Rs 600 million authorized capital, Rs 466.8 million of issued capital and Rs 455 million of paid-up capital. It has an objectives of extending professionalized and efficient banking services to various segments of the society. The bank had an initial paid up capital of Rs 3 Crore. Today the bank has grown to become one of the leading banks in Nepal. We at EBL believe that the long term development of an organization depends on how we build trust among our stakeholders. Our values are focused on the ethics at work place and outside. Thus we need to be as transparent as possible through proper corporate governance. We have built a code of conduct where by all employees working, needs to follow it stringently. The bank has been conferred with „Bank of the Year 2006, Nepal‰ by the banker, a publication of financial times, London. The bank was bestowed with the NICCI Excellence award twice in 1999 and 2003 by Nepal India chamber of commerce for its spectacular performance under finance sector.

Himalayan Bank Ltd

Himalayan Bank Ltd. is a joint venture bank with Habib Bank Ltd. of Pakistan which was established in18 june1993 under the company act 1994. This is the first joint venture bank holding with maximum share by Nepalese private sectors. Its ownership is composed of financial institutions of Nepal by 66.29%, Habib Bank Ltd. of Pakistan by 20% and general public of Nepal by 13.58%. Currently bank has Rs 1000 million of authorized capital and Rs 600million of issued. The fast growth of the banks has been made possible through the strategic approach they undertaken and the years of hard work and perseverance on the part of the Board, top management and

qualified human resources. Any business opportunities that have come along has been thoroughly evaluated and tapped when ever found feasible. This has put info use all available forms of resourced to grab the opportunities available in the banking sectors.

Nabil Bank Ltd (Nabil)

The first joint venture bank, Nabil bank Ltd was established with technical service agreement in the country in 1984 under the management of Dubai Bank Ltd., United Arab Emirates. Its ownership structure consists of 50% share from Dubai Bank Ltd., 20% share from financial institutions of Nepal and rest 30% share from the general public. Its initial paid up capital was Rs. 30 million. At present, its capital structure consists with authorized capital 200 Million, issued capital 69 Million and paid up capital 69 Million. 50% of the share is in the name of foreign partner NB International, Ireland. Today the Bank has established itself as the Bank of 1st Choice. It is the largest bank in terms of the network and number of branches amongst the commercial banks with a wide network of ATMs and offerings including a angel of diversified service products. they have a number of domains in their precedence of excellence that mirrors Where we stand in the market.

Standard Chartered Bank Nepal Limited (SCBNL)

Nepal Grindlays Bank, second joint venture bank was established with 50% equity share with foreign partner ANZ Grindlays Bank PLC, 33.341% of Nepal Bank Ltd and 16.659% of Nepali public in 1987. Its initial paid up capital was Rs. 30 Million. The bank is known presently as Standard Chartered Bank. Today the Bank is an integral part of Standard Chartered Group who has 75% ownership in the company with 25% shares owned by the general public. The paid up capital is Rs.62 Million at present. Nepal Rastra Bank erased entry restriction with an amendment to the commercial Bank Act in 1980 and Government adopted liberal and market oriented economic policy after the restoration of Democracy in 1990. Joint venture banks are attracted to open commercial banks in the country. The following commercial banks are in operation at present.

1.5. Statement of Problem

In the present context no. of commercial banks are growing in Nepal as most of the commercial banks are able to earn profit every year and their expansion also being

rapidly. The NRB has set rule to spread banking service not only to urban area but also to remote area so commercial banks are widening its services in village area too. It shows the banks are not only profit oriented they are committed to the economic development of the country also. But most of the functions of commercial banks are still concentrated on the profit. In the present context also the spreading branches to remote area is becoming just formality and support the NRB rule. In this context the thesis will concentrate its study on the following areas;

i. What are the dividend practices of commercial banks?
ii. What are determinants of dividend payment of Nepalese commercial banks?
iii. What is the existing situation of EPS, DPS, Payout Ratio, MPPS, P/E ratio, EY and DY of sampled commercial banks?

1.6 Objectives of the Study

The major objective of the study is to analyze current dividend policy and and practices of Nepalese commercial banks. The specific objectives of the study are as follows:

a. To describe dividend practices of the commercial banks.
b. To examine determinants of dividend payment of Nepalese commercial banks.
c. To analyze EPS, DPS, Payout Ratio, MPPS, P/E ratio, EY and DY of samples banks?

1.7 Rationale of the Study

Banking and financial institutions are the vital sectors for the economic growth of any country. The banking and financial sectors are the backbone of the economic development of the country as it provides the huge amount of capital for the infrastructure development and overall upliftment of the economic condition of the country. Any study in this sector will helpful for several stakeholders of this sector. Researcher believes that following institution and individual will be benefited from the study covering dividend of commercial banks of Nepal:

- Individual who will carryout further research work in dividend and dividend policy of any banking and financial sectors.

- The existing and upcoming stakeholders of commercial banks of Nepal who have keen interest on the dividend of commercial banks.
- Individuals who have keen interest in Nepalese banking & financial sector and institutions related to the topic.

1.8 Limitations of the Study

The study and outcome of the study has been an individual effort. As the study will be based on data of commercial banks of Nepal the research may not be fit for the other development banks of Nepal and financial institutions. The weakness or limitations of the study can be pointed out as follows:

a) The study has been based on major secondary data; therefore, the accuracy of results and conclusions highly depends upon the reliability of these data.

b) As the title specifies the study covers about dividend subject only other factors beside it has not be covered by the study.

c) Due to constraints, the study covers only past last five years & selected sample banks.

d) Due to the small sample size, it may not fully represent Nepal as a whole.

1.9 Plan of the work

The research is the initial stage of the research work and research report writing. It gives the way to the successfully completion of the research project It is the blue print of the research to be done or a small model of the research report that to be prepared on the completion of the research on the selected topic. Finally after completion of the research work, research has been divided into five chapters:

Chapter I – This is the introduction section covers the background of the study, the introduction to sample institutions selected for study, objectives & limitations as well as statement of problem and rationale of the study which gives the importance, area coverage and strengths & weakness of the selected topic.

Chapter II – This section literature review, which covers the citation of the previously conducted research work on the same field as well as review of the books, articles related to the capital structure.

Chapter III – This section is named as research methodology which gives the brief introduction of the methods that applies for research work in order to get the result of the study.

Chapter IV – In this section of research report contains the data presentation, analysis, interpretation related to the research problem based on the annual reports of joint venture commercial banks of Nepal.

Chapter V – Last but not the least, the final section of the research report is summary, conclusion and recommendation on which the total findings of the study has been summarized point wise as well as the conclusion of the research work and recommendations if any.

CAPTER II

REVIEW OF LITERATURE

This chapter covers the review of concerned literatures relevant to the dividend policy. While reviewing the literature, different books, studies of magazines, articles, Journals and unpublished dissertation have been used. This chapter is presented in to two parts-theoretical review and research review.

2.1 Conceptual Framework

Dividend refers to that portion of a firm's net earning, which are paid out to the shareholders (Khan & Jain: 1999).Dividend means a share of profits paid to people who own the parts of a company. In other word it can be understood as the profit of earning made by the firm that is distributed to the shareholders in return of their investment in shares. Profit maximization is the main objective of the entire firm. While making the profit the firm has two alternatives, the first alternative related to determine how much amount of profit to be retained in the firm for business expansion and other alternative tells the amount of the money distributed to its investors (shareholders). It is necessary to maintain the balance between there two alternative. Most of the firms' intense is try to make balance between them. For this they retain certain percentage of profit in business and rest is distributed to the stockholders as dividend

Dividend Policy determines the division of earnings between payments to stockholders and reinvestment in the firm. Retained earnings are one of the most significant sources of funds for financing corporate growth, but dividends constitute the cash flows that accrue to stockholders (Weston, & Copeland: 1990). Higher payment of dividend helps to attract the new investor. But it is most challenging job to decide portion of dividend to be paid to shareholders along with the management of fund for expansion of firm. It is seemed that an effective dividend policy is required to overcome from the problem of how much amount should be retained and how much should be paid to the shareholders. The dividend policy includes all aspects related to the payment of dividend. Dividend policy is the policy of any firm/company regarding the division of its profit between

shareholders as dividend and retention of the profit for making investment. Dividend policy involves the decision to pay out earning versus retaining them fir reinvestment in the firm. Any change in dividend policy has both favorable and unfavorable effects on the firm's stock price. Higher the dividends means higher the immediate cash flows to investor, which is good, but lower future growth, which is bad. The dividend policy should be optimal which balances the opposing forces and maximizes stock price. The policy of a company in segmentation of its earning as dividend and as retention for its investment is known to be dividend policy. Dividend policy may consider as one of the essential decision to maximize the value of common stock as it directly affects the structure of the firm, the flow of funds, corporate liquidity and investor's attitude. There fore management should trey to maintain regular dividend. For regular dividend, the firm will have sufficient earning. Management will set a lower regular dividend rate than firms with the same average earnings but less volatility. Management may also declare extra dividends in years when earning are high and funds are available. It determines the ratio of earning to be retained and payout. As the dividend payment and retained earning have inverse relationship, the entire problem relating dividend payment and retention of earning is closely examined before applying appropriate dividend policy. The firm pays higher dividend in wealth maximization objective but in the objective of the expansion of the firm, the principle of lower payout should be adopted. Most of the investors expect to continue in each year as well as to receive price when they sell the stock Weston & Brigham: 1989).

Dividend assists as a simple tool of management interpretation of the firm's recent performance and its future prospects. Some companies use to pay whole earning as dividend at the beginning to create good image in commercial field but later, they may change their policy and pay certain percent of dividend. It is considered that dividend policy should be concerned with the well being of the shareholder, which can be partially measured by dividend received but more accurately measured in terms of the market value of the stock.

2.1.1 Major Forms of Dividend

Dividends are the distribution of a company's gains over a fixed period of time to shareholders. This disbursement of capital is done so under the authority of the board of directors. Dividends are issued on a per share basis and is called a per share dividend. The portion of dividend payout will fluctuate from period to period by making support in the amount of acceptable investment opportunity available to the firm. Dividend can be paid to the shareholders in various forms depending upon the objectives and policies implemented by a firm. A firm must ensure the smooth growth of the firm as well as satisfy the expectation of the shareholders before adopting any dividend policy. The corporations in Nepal are in the early stage of development due to which they need to pay extensive concentration in the dividend policy. In Nepalese context, cash dividend and stock dividend and are the most popular form of dividend payment. When the firm doesn't have sufficient cash, it pays different forms of dividend to its investors. Besides cash and stock dividend, scrip dividend, property dividend, bond dividend can also be paid as the return of the investors (Shareholders).

(1) Regular Dividend

By dividend we mean regular dividend paid annually, proposed by the board of directors and approved by the shareholders in general meeting. It is also known as final dividend because it is usually paid after the finalization of accounts. It sis generally paid in cash as a percentage of paid up capital, say 10 % or 15 % of the capital. Sometimes, it is paid per share. No dividend is paid on calls in advance or calls in arrears. The company is, however, authorized to make provisions in the Articles prohibiting the payment of dividend on shares having calls in arrears.

(2) Cash Dividend

By its name, cash dividend refers to the portion of earning paid to the investors in the form of cash in proportion to their share investment in the company. In context of Nepal, cash dividend is the most popular form of dividend and is mostly adopted by many companies/forms/financial institutions. When cash dividend is paid, the cash account and the reserve account of a company will be reduced, thus both the total assets and the net worth of the company are reduced as well when cash dividend is distributed. A company

must arrange sufficient cash at the time of dividend payment in cash. When a company follows a stable dividend payment policy, it should prepare cash budget for a coming period to indicate the necessary funds which would be needed to meet regular dividend payment of the company (Pandy: 1999).

(3) Interim Dividend

If Articles so permit, the directors may decide to pay dividend at any time between the two Annual General Meeting before finalizing the accounts. It is generally declared and paid when company has earned heavy profits or abnormal profits during the year and directors which to pay the profits to shareholders. Such payment of dividend in between the two Annual General meetings before finalizing the accounts is called Interim Dividend. No Interim Dividend can be declared or paid unless depreciation for the full year (not proportionately) has been provided for. It is, thus,, an extra dividend paid during the year requiring no need of approval of the Annual General Meeting.

(4) Stock-Dividend

Companies, not having good cash position, generally pay dividend in the form of shares by capitalizing the profits of current year and of past years. Such shares are issued instead of paying dividend in cash and called 'Bonus Shares'. Basically there is no change in the equity of shareholders. Certain guidelines have been used by the company Law Board in respect of Bonus Shares

(5) Scrip Dividend

Scrip dividends are used when earnings justify a dividend, but the cash position of the company is temporarily weak. So, shareholders are issued shares and debentures of other companies. Such payment of dividend is called Scrip Dividend. Shareholders generally do not like such dividend because the shares or debentures, so paid are worthless for the shareholders as directors would use only such investment is which were not . Such dividend was allowed before passing of the Companies (Amendment) Act 1960, but thereafter this unhealthy practice was stopped.

(6) Bond Dividends

In rare instances, dividends are paid in the form of debentures or bounds or notes for a long-term period. The effect of such dividend is the same as that of paying dividend in scrip. The shareholders become the secured creditors are the bonds has a lien on assets.

(7) Property Dividend

Sometimes, dividend is paid in the form of asset instead of payment of dividend in cash. The distribution of dividend is made whenever the asset is no longer required in the business such as investment or stock of finished goods.

(8) Special Dividend

Companies with wasting assets may declare this kind of dividend, by those wishing to retrench operations and by those winding up their corporate existence. Cash dividends, in such cases are considered as a return of capital in gradual stages

(9) Optional Dividend

Optional dividends are payable in cash or stock at the option of stockholders. Sometimes cash dividends are applied towards the purchase of new stock unless the stockholder expresses his/her desire to have cash.

(10) Depression Dividend

Depression dividends may arise from reduction in stated capital. A corporation thus wipes out its deficits and creates surpluses in order to keep up dividend payments. Unintelligent and indifferent stock holders lend their approval to such hocus-pocus.

(11) Dividends from Appreciation

When assets are disposed of for more than the book value, dividends may be paid out of the realized appreciation.

(12) Liquidation Dividend

Liquidation dividends represent the distribution of assets as a result of the failure of a company or on its dissolution. They are paid out of properties that are surrendered for cash or some other form of wealth. Liquidation dividends may be paid to bond-holders as well as to stockholders.

2.1.2 Commercial Bank in Nepal

An institution which accepts deposits, makes business loans, and offers related services. Commercial banks also allow for a variety of deposit accounts, such as checking, savings, and time deposit. These institutions are run to make a profit and owned by a group of individuals, yet some may be members of the Federal Reserve System. While commercial banks offer services to individuals, they are primarily concerned with receiving deposits and lending to businesses.

Commercial Bank Act, 2031 B.S. of Nepal has defined it as a commercial bank is one which exchanges money, deposits money, accepts deposits, grants loans and performs commercial banking functions and which is not a bank meant for co-operative agriculture, industries or for such specific purpose. The Commercial Bank Act 2031 also pointed the functions of commercial banks commercial banks provide short term debts necessary for trade and commerce. They take deposits from the public and grants loans in different forms. They purchase and discount bills of exchange, promissory note, and exchange foreign currency. They discharge various functions on behalf of their customers provided that they are paid for their services.

The first Commercial Bank of Nepal is Nepal Bank Ltd. This was established in 1994 B.S. After the establishment of it, Rastriya Banijya Bank on 2022 B.S. and Agriculture Development Bank were established. After the restoration of multi party democracy in Nepal, government took liberal economic policy. As a result, a large number of commercial banks were established in joint venture with foreign commercial banks. Nepal bank Ltd. And Rastriya Banijya bank has branches in most of the districts. As per the provision of the liberal policy adopted in Nepal, several banks are established in the different places of the country. On the permission of central bank, commercial bank can

be established o any time anywhere. On the permission of central bank, development banks are also performing limited commercial functions. It performs the work of bridge between the purchase and sale of capital so that it does not allow to have shortage of capital in both the sides. It is so popular in the world because it accepts deposits from the clients who have more unused amount and provides capital to those who wants to do productive work in teams of loan.

2.1.3 Dividend policy and Commercial Bank

In many cases, companies choose to explicitly state the provisions within the dividend policy. This is definitely to the advantage of the shareholder, as a well defined policy makes it much easier to project the amount of payout profits generated for the period under consideration and thus be able to determine the size of the dividends that will be issued. When the dividend policy is well defined and documented, it is easy for the shareholder to obtain a written copy and thus be fully informed as to how the policy works. However, there are cases where the dividend policy is not so well documented. When this is the case, investors sometimes base their assumptions on upcoming dividend payments on what has occurred in the past. While less systematic, it is still possible to project a more or less accurate estimate of what the dividend payout will actually be. In cases where the dividend policy is not specifically defined, investors often look at the history to spot any trends that emerged in the past. If the dividend payments have been more or less constant for the last several years, and there has been no loss in business volume, it is reasonable to assume the payments will still be in the same general range as before. However, if the dividend history is more volatile, the shareholder may attempt to identify what factors led to the up and down movement of the dividends and determine if any of those factors are relevant to the current dividend period.

In both expressed and implied dividend policy procedures, it is less common for the dividends to be increased. Part of the reason for that is companies tend to look closely at retained earnings and want to make sure the increased level of earnings will be sustained over the long term. Once this upward trend is deemed to be more or less permanent, the company may choose to increase dividends. Far more common is the practice of reducing

dividends. This usually takes place because there is a decrease in the company's business volume that is not anticipated to be recaptured in the foreseeable future. At other times, the decrease may be due to the need to retain more cash on hand for capital expenses. In both these scenarios, companies tend to notify the shareholders in advance that these factors exist and a chance in dividends will take place in order to meet the challenge to remain profitable. There is no any specific consideration determined by the Nepal government about dividend payment for commercial banks specifically. Government has developed some rules regarding dividend policy for companies under Nepal company act 2053B.S. So the same rules have been adopting by Nepalese commercial banks in the regard of decision making of dividend payment to investor, which can be sited below.

In Company Act 2021, nothing was explained about dividend practice in Nepal but after the set up of Security Exchange Act 1983, Nepal Stock Exchange Limited which preserved the investor's interest. Then, some legal provision for dividend payment mentioned in Nepal Company Act 1997 :(Endi Consultants Research Group 1997, p. 43).

Section 2 (M) states that bonus shares (stock dividends) means shares issued in the form of additional shares to share holders by capitalizing the surplus from the profits or the reserve fund of a company. The term also denotes an increase in the paid up values of the shares after capitalizing surplus or reserve funds (Endi Consultants Research Group: 1997). Section 47 has prohibited company from purchasing is own shares. This section states that no company shall purchase its own shares or supply loans against the security of its own shares (Endi Consultants Research Group: 1997).

- ✓ Section 134 Bonus Shares and Sub Section (1) states that the company must inform the office before issuing bonus shares. Under Sub Section (1), this may be done only according to a special resolution passed by the general meeting (Endi Consultants Research Group: 1997).
- ✓ Section 140: Dividends and Sub Sections of this Section are as follows;(Ibid)

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

- ✓ Sub Section (2): In case dividends are not distributed within the time limit mentioned in Sub Section (1), this shall be done by adding interest at the prescribed rate.
- ✓ Sub Section (3): Only the person whose name stands registered in the register of existing shareholder at the time the dividend shall be entitled to.

2.2 Passive versus Active Dividend polices

Dividend as a Passive Residual

Can the payment of cash dividends affect shareholder wealth and, if so, what dividend-payout ratio will maximizes shareholder wealth? As did when studying the effects of financial leverage, again assume that business risk is held constant. To evaluate the question of weather the dividend-payout ratio effects shareholder wealth, it is necessary to first examine the firm's dividend policy as solely a financing decision involving the retention of earnings. Each period, the firm must decide whether to retain its earnings or distribute part of all of them to shareholder as cash dividends. (rule out share repurchase for now.) as long as the firm is faced with investment projects having returns exceeding those that are reputed (i.e., positive-NPV projects), the firm will use earnings, plus the amount of senior securities the increase in the in the equity base will support, to finance these projects if the firm has earnings left after financing all acceptable investment opportunities, these earnings would then be distributed to shareholder in the form of cash dividends. If not, there would be no dividends. if the number of acceptable investment

opportunities involves a total amount that exceeds the amount of retained earnings plus the senior securities these retained earnings will support, the firm would finance the excess needs with a combination of a new issue and senior securities.

When institution treat dividend policy issue as strictly a financing decision, the payment of cash dividends is a passive residual. The percentage of earnings paid out as dividends will fluctuate from period to period in keeping with fluctuation in the amount of acceptable investment opportunities available to the firm. If these opportunities abound, the percentage of earnings paid out is likely to be zero. On the other hand, if the firm is unable to find profitable investment opportunities, dividends paid out will be 100 percent of earnings. For situation between these two extremes, the dividend-pay out ratios will be a fraction between zero and one.

The treatment of dividend policy as a passive residual, determined solely by the availability of acceptable investment proposal, implies that dividends are irrelevant. Are dividends really just a means of distributing unused funds? Instead, should dividend payments be an active decision variable with earnings retentions, it must examine the argument that dividends are irrelevant, which means that change in the dividends- payout ratio(holding investment opportunities constant) do not affect shareholder wealth.

a) Irrelevance of dividends

Miller and Modigliani (M&M) provides the most comprehensive argument for the irrelevance of dividends (Merton H. Miller and Franco Modigliani: 1961: 411-433). They assert that, given the investment decision of the firm, the dividend-payout ratio is a mere detail and that it does not affect the wealth of shareholders. M&M argue that the value of the firm its determined solely by the earning power of the firm's assets to its investment policy; and that the manner in witch the earnings stream is split between dividends and retained earnings does not affects this value. As we pointed out earlier, when the financial firm considered the capital structure decision, M&M assume\me perfect capital markets where there are no transactions costs, no flotation cost to companies issuing securities, and no taxes. Moreover, the future profits of the fir are assumed to be known with certainty. (later this last assumption will be removed.)

Current dividends versus Retention of Earning

The crux of M$M's position is that the effect of dividend payments on shareholder wealth is exactly offset by other means of financing. Let us first consider selling additional common stock to raise equity capital instead of simply retains earnings. After the firm has made its investment decision, it must decide whether (1) to retain earnings or (2) to pay dividends and sell new stock in the amount of these dividends in order to finance the investment. M&M suggest that the sum of the discounted value per share of common stock after financing plus current dividends paid id exactly equal to the market value per share of common stock before the payment of current dividends. In other words, the common stock's decline in market price because of the dilution caused by external equity financing is exactly offset by the payment of the dividend. Thus the shareholder is said to be indifferent between receiving dividends and having earnings retained by the firm.

Conservation of value

Given M&M's assumption of certainty and perfect capital markets, the irrelevance of dividends naturally follows. As with our example for corporate financing leverage in the previous chapter, the total-value principal ensure other than the sum of market value plus current dividends of two firms identical in all respects other than dividend-payout ratios will be the same.

Investors are able to replicate any dividend stream the company might be able to pay but currently is not. If dividends are lower than desired, investors can sell some share of stock to obtain their desired cash distribution. If dividends are higher than desired, investors can use dividends to purchase additional share of stock in the company. Thus investors are able to manufacture "homemade" dividends in the same way that they could devise "homemade" financial leverage if they were unhappy with a firm's current capital structure. for a corporate decision to have value, the company must be able to be do something for shareholders that they cannot do themselves. Because investor can manufacture homemade dividends, which are perfect substitutes for corporate dividends under the preceding assumptions, dividend policy is irrelevant. As a result, one dividend policy is as the next. The firm is unable to create value simply by altering the mix of

dividends and retained earnings. As in capital structure theory, there is a conservation of value so that the sum of the parts is always the same.

Modigliani and Miller's Study

According to Modigliani and Miller, dividend policy of a firm is irrelevant as it doesn't affect the wealth of the shareholders (Miller & Modigliani: 1961: PP.411-433). In other words, the division of earnings between dividend and retained earning is irrelevant from shareholders viewpoint. This is the most comprehensive argument for the irrelevant of the dividend. In their 1961 article, for the first time in the history of finance, Modigliani and Miller advocated that dividend policy does not affect the value of the firm i.e. dividend policy has no effect on the share price of the firm. They argued that the value of the form depends on the firm's earnings which depend on its investment policy. Therefore there is no significant relationship between dividend policy and value of firm. In other words a firm's value is independent of dividend policy.

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

a. The firms operate in perfect capital market where all investors are rational and information is freely available to all. Securities are infinitely divisible and no investor is large enough to influence the market price of securities.
b. There are no flotation costs. The securities can be purchased and sold without payment of any commission or brokerage etc.
c. Taxes do not exist. Alternatively, there are no differences in tax rates applicable to capital gains and dividends.
d. The firm has a fixed investment policy, which is not subject to change.
e. Risk of uncertainty does not exist. Investors are also able to forecast future prices and dividends with certainty, and one discount rate is appropriate for all securities and all time periods.

The proof of the support of the argument is discussed as below:

Step 1: The market price of the share in the beginning of the period 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,

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

Where,

P_o = Market price at the beginning or at the zero period.

Ke = Cost of the equity capital

D_1 = Dividend per share to be received at the end of period one.

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

Step 2: The market value of the firm can be calculated as follows when the firm doesn't resort any external or new financing. (Multiplying both sides of equation 1 by the number of shares outstanding (n) to obtain the total value of the firm)

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

Where,

n= Number of the equity shares outstanding at the zero period.

Step 3: If the firm's internal source financing all short of the funds required to meet its investment opportunities then the firm issues new shares to finance the new investment needs of funds at a price of P1, the value of the firm at time zero will be:

$$nPo = \frac{nD_1 + P_1(n+Dn)-DnP1}{1+Ke}$$

Where,

n= no. of shares at the beginning

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

Step 4: If the firm were to finance all investment proposals, (either of retained earning or the issuance of new shares or both) the total amount of the new share issued would be given below.

$DnP_1 = I – (E – nD_1)$

Or, $DnP_1 = I – E + nD_1$

Where,

DnP_1 = the amount obtained from the sale of new shares to finance capital budget.

I = the total amount requirement of capital budget.

E = Earning of the firm during the period

$E – nD_1$ = Retained Earning

Step 5: By substituting the value of DnP_1 from the equation of step 4 to equation of step 3, we find,

$$nPo = \frac{nD_1 + P_1 (n+Dn) – I + E – nD_1}{1 + Ke}$$

or, $$nPo = \frac{P_1 (n + Dn) – I + E}{1 + Ke}$$

Conclusion

As stated earlier MM assumption tells that dividend policy has no effect on the share price. In other words MM conclude that dividend policy is irrelevant and it has no effect in the value of the firm. So the role of dividend can't be shown on above equations.

MM approach does not seem so relevant to apply in Nepalese context. Because when we apply this approach, the assumptions supposed by MM are significantly deviated. We are unable to find the rational investors as well as perfect capital market in Nepal, which are considered by MM. It's also not seemed so sound to neglect the flotation cost, transaction cost and tax effect on capital gain as neglected by MM. A conscious investor always

finds difference between dividend and retained earning. Arbitrage arguments as explained by MM apply only when there are very sensitive investors and which are lacking in Nepal. Thus, MM approach is not relevant in the case of Nepal.

b) Arguments for Dividend Relevance

A number of arguments have been advanced in support of the contrary position, namely, that dividends are relevant under conditions of uncertainty. In other words, investors are not indifferent as to whether they receive returns in the form of dividend income of share price appreciation. Firm shall examine these arguments under conditions of uncertainty.

Preference for Dividends

Certain investors may have a preference for dividends over capital gains. The payment of dividends may resolve uncertainty in their minds concerning company profitability. Dividends are received on a current, ongoing basis, whereas the prospect of realizing capital gains is in the future. Therefore investors in dividend-paying company resolve their uncertainty earlier than those investing in a non-dividend-paying company. To the extent that investors prefer the early resolution of uncertainty, they may be willing to pay a higher price for the stock that offers the greater dividend, all other things held constant. If, in fact, investors can manufacture “homemade” dividends, such a preference is irrational. Nonetheless, sufficient statements from investors make it difficult to dismiss this argument. Perhaps, for either psychological reasons or reasons of inconvenience, investors prefer mot to manufacture “homemade” dividends but to get the “real thing” directly from the company.

Taxes on the Investor

When firm allow for taxes, there are a variety of effects. To the extent that the personal tax rate on capital gains is less than that on dividend income, there may be an advantage to the retention of earnings. In addition, the capital gains tax is deferred until the actual sale of stock (when any gain is realized). Effectively, the shareholder is given a valuable timing option when the firm retains earnings as opposed to paying dividends. This would suggest that a dividend-paying stock will need ro provide a higher expected tax return than non-dividend-paying stock of the same risk. According to this notion, the grater the

dividend yield on a stock, the higher the required before-tax return, all other things being the same.

If there are clienteles of investors having different dividend preference, companies could adjust their dividend-payout ratio to take advantage of the situation. Suppose that two-fifth of all investors refer a zero dividend-payout ratio, one-fifth prefer a 25 percent payout ratio, and the remaining two-fifth prefer 50 percent payout ratio,. If most companies pay out 25 percent of their earnings in dividends, there will be excess demand for the shares of companies paying zero dividends and for the shares of companies whose dividend-payout ratio is 50 percent. Presumably, a number of companies will recognize this excess demand and adjust their payout ratios to increase share price. The action of these companies will eliminate the excess demand. In equilibrium, the dividend-payout ratios of companies will match the desires of investor groups. At this point, no company would be able to affect its share price by altering its dividend. As a result, even with taxes, the dividend- payout ratio would b irrelevant.

In actuality, firms are left with an unsettled situation I which the effect of taxes on dividends is not clear. Before considering some of the empirical evidence on the effect that dividends have on share price. The firm must look at other factors that may influence the payment o dividends.

Flotation Cost

The irrelevance of the dividend payout is based on the idea that, when favorable investment opportunities exist and yet dividends are paid, the fund paid out of the firm must e replaced by funds acquired through external financing. The introduction of flotation cost involves with external financing favors the retention of earnings in the firm. For each rupee paid out in dividends, the firm nets less than a rupee after flotation costs per rupee of external financing.

Transaction Cost and Divisibility of Securities

Transactions costs involved in the sale of securities tend to restrict the arbitrage process in the same manner as that described for debt. Securities who desire current income must pay brokerage fees on the sale of portions of their stock ownership if the dividend paid is not sufficient to satisfy their current desire for income. This fee, per rupee of shares sold, varies inversely with the size of the sale. For a small sale, The brokerage fee can be a rather significant percentage of te total sale. As a result of this fee, shareholders with consumption desires in excess of current dividends will prefer that the company pay additional dividends. Perfect capital markets also assume that securities are infinitely divisible. The fact that the smallest equity-security unit is one share may result in 'lumpiness' with respect to selling shares for current income. This, too, acts as a deterrent to the sale of stock in lieu of dividends. On the other hand, shareholders mot desiring dividends for current consumption purposes will need to reinvest their dividends. Hence, again, transactions costs and divisibility problems work to the disadvantage of the shareholder, although this time as a deterrent to the purchase of stock. Thus transactions costs and divisibility problems cut both ways , and one is not able to draw directional inferences regarding paying dividends versus retaining earnings.

Financial Signaling

Financial signaling is different from the other arguments presented on this section in that it depends on imperfections on the market for financial information. It suggests that dividends have an impact on share price because they communicate information, or signals, about the firm's profitability. Presumably, firms with good news about their future profitability will want as tell investors. Rather than make a simple announcement, dividends may be increased to add conviction to the statement. When a firm has a target dividend-payout ratio that has been stable over time, and the firm increase this ratio, investors may believe that management is announcing a positive change in the expected future profitability of the firm. The signal to investors is that management and the board of directors truly believe that thing are better than the stock price reflects.

Accordingly, the price of the stock may react favorably to this increase in dividends. The idea here is that the reported accounting earnings of a company may not be proper

reflection of the company's economic earnings. To the extent that dividends provide information on economic earnings not provided by reported earnings, share price will respond, put another way, cash dividends speak louder than words. Thus dividends are said to be used by investors as predictors of the firm's future performance dividends convey management's expectations of the future.

Gordon's Model

Another concept developed by Myron J. Gordon in 1962. This theory assumes that investor gives more emphasis to the present dividend more than future capital gain. So this theory is called Bird in the hand theory. This model insists that an increase in dividend payout ratio leads to increase in the stock price for the reason that investors consider the dividend yield is less risky than the expected capital gain. This model explains that investors are indifferent between current dividend and retention of earning.

This model is based on following assumptions:

The firm is an all equity firm

No external financing is available

Internal rate of return (r) and cost of capital (k) are constant

The corporate tax rate doesn't exist

The retention rate (b), once decided upon, is constant

Cost of capital must be greater than growth rate Based on above assumptions, market value of shares can be determined by using following formulae:

$$P = \frac{K(1-b)}{K - b.r}$$

Where,

P = Market price of Shares

K = Cost of capital

b = Retention ratio

r = Growth rate / Rate of return

By solving above equitation, we can find three stages of a firm:

If the firm is in growth stage, the share price will decline in corresponding with increased in payout ratio or decrease in retention ratio i.e. high dividend payout ratio results to decrease in market price of share. Hence, there is positive relationship between retention ratio and share price in growth firm.

If the firm is in normal stage, there will be no any change in share price regarding change in payout ratio. It means dividend and stock price are free from each other in normal firm.

If the firm is in declining stage, the share price will rise in correspondence with increase in dividend payout ratio. Hence there is negative relationship between retention ratio and stock price in declining firm.

Walter's Model

Professor Walter conducted a study on dividend policy and common stock prices in 1966, arguing that dividend policy almost always affects the value of the enterprise. According to him, the dividend policy of the firm affects the value of the shares, so the dividends are relevant. In the view of Professor Walter Investment policy and Dividend policy are correlated to each other. The importance of the relationship between internal rate of return (R) and its cost of capital (k) in determining the dividend policy is clearly shown in his study.

Assumptions of this model are as follows:

i) he firm survives in infinite life.
ii) Either the firm distributes entire earnings as dividend or immediately reinvested
iii) Internal rate of return (r) and cost of capital (k) remain constant.

iv) The value of EPS and DPS are assumed to remain constant forever in determining a given value.

v) The firm finances all investment through retained earning. There is no need of debt or new equity shares.

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

$$P = \frac{DPS}{Ke} + \frac{r/k_e(EPS-DPS)}{k_e} \quad \text{or} \quad P = \frac{DPS+r/k_e(EPS-DPS)}{k_e}$$

Where,

P = Market price per share

DPS = Dividend per share

EPS = Earning per share

R = Internal rate of return

Ke = Cost of capital

In the opinion of Walter, optimum relationship between firm's internal rate of return(r) and its cost of capital (k) results optimum dividend policy for the firm. Different dividend policies for the different types of the firms suggested by Walter are discussed below:

a. Growth Firm (r>k)

The firms which expand rapidly are known as growth firms. Because of the ample investment opportunities, these firms enjoy reinvesting their earning at the rate which is higher than the rate expected by shareholders. So, firms having r>k is referred as growth firms which yielding return (r) is higher than the opportunity cost of capital (k). They will maximize the value per share if they follow a policy of retaining all earnings for internal investment. For such a firm dividend payout ratio is zero and correlation between dividend and stock price is negative. The market value per share (P), increases as payout ratio decreases when r>k.

b. Normal Firm (r=k)

When the firm's required rate of return and cost of capital are equal, those firms used to be called normal firm. In such model, market value per share would be unaffected by the dividend payout ratio; i.e. dividends are indifferent from the stock price. In normal firms, whether company retains the profit or distributes it as dividend could not make any difference. The market price of share will remain constant for different dividend payout ratio from zero to 100. Thus there is no unique optimum payout ratio for a normal firm. One dividend policy is as good as other and the market value per share is not affected by the payout ratio when r=k.

c. Declining Firm (r<k)

If the firms don't have any profitable business opportunities, their investment rate would be less than required rate of return. The investors would expect to get earning as dividend so that they could spend elsewhere with higher return than declining firm. In these firms, the relation between dividend and stock price is positive. So, by distributing the entire earnings as dividend, the value of the share will be at its optimum level. In other words, the market value per share of a declining firm with r<k will be maximum when it does not retain its earnings at all. To maximize the value of share, dividend also should be maximized. The optimum payout ratio for a declining firm is 100% and the market value per share increases as payout ratio increases when r<k.

Walter's model concludes that the dividend policy of a firm depends on the availability of investment opportunities and the relationship between the internal rate of return and cost of capital of the firm.

This model has the following Limitations:

a) No external financing: Walter's approach assumes that retained earning finance is the only investment opportunity of the firm and no external financing debt or equity is used for the financing. When such a situation exists, either the firm's investment or its dividend policy or both will be sub-optimum. This means when the firm's earning aren't adequate to exploit all the investment opportunities having return at equal or more than cost of capital, this approach doesn't allow financing the gap by using other sources.

b) Constant ‘r’ and ‘k’: Walter’s approach is based on assumption that rate of return (r) and opportunity cost of capital or discount rate (k) are constant. In fact ‘r’ decreases as more investment occurs and ‘k’ changes directly with the firm’s risk. This model may not be applicable in case of Nepalese companies because of his other assumption i.e., EPS, DPS etc are constant.

2.3 Dividend Payout Schemes

Stability or regularity of dividends is considered as a desirable policy by the management of companies. Most of the shareholders also prefer stable dividends because all oter things being the same, stable dividends have a positive impact on the share. By stability , we mean maintain g its position in relation to a trend live preferably one that is upward sloping. Three of the commonly used dividend policies are:

a) Constant Dividend Per share

Constant dividend policy is based on the payment of a fixed rupee dividend in each period. A number of companies follow the policy of paying fixed amount per share as dividend every period, without considering the fluctuation in the earnings of the company. This policy doe mot implies that the dividend per share or dividend rate will never be increased. When the company reaches new level of earning and expects to maintain it the annual dividend per share may be increased. Investors who have dividends as the only source of their income prefer the constant dividend policy.

b) Constant Payout Ratio

The ratio of dividend to earning is known as payout ratio. When fixed percentage is as dividend in every period, the policy is called constant payout ratio. Since earning fluctuates, following this policy necessary means that the rupee amount of dividend will fluctuate. It ensures that dividends are paid when profits are earned, and avoided when it incurs losses.

c) Low Regular Dividends Plus Extra

The policy of paying a low regular dividend plus extras is a compromise between a stable dividend (or stable growth rate) and a constant payout rate. Such a policy gives the firm flexibility, yet investors can count on receiving at least a minimum dividend. It is often followed by firms with relatively volatile earnings from year to year. The low regular dividend can usually be maintained even when earnings decline and extra dividend can be paid when excess funds are available.

d) Residual Theory of Dividend

According to this theory, "the dividend is distributed if there exists a balance earning after paying fixed obligations and investment opportunities (Pandey: 1999). This theory tells only left after earnings should be distributed to the shareholders in the form of dividend after accepting all the profitable investments opportunities in accordance with the firm's investment policy. The firm must invest in such project, which have greater than required and only residual amount of earning should be distributed to the stockholders as the form of cash dividend.

Dividend amount wouldn't remain constant in every time because the firm usually gets investment opportunity in profitable securities. It must prefer retained earning instead of external funding because external funding is quite expensive in comparison with internal funding due to flotation cost and others. When the firm uses huge amount of earning for its expansion, the dividend payout to its stockholders would certainly be bit lower. Although the residual theory of the dividend appears to make further analysis of the dividend policy unnecessary, it is not clear that dividends are solely a means of disbursing excess funds (Rao: 1992).

In a bird's eye view, it can be conclude that dividend amount of the firm can be determined by investment opportunity as well as availability of the internally generated fund of a firm.

2.4. Factors Affecting Dividend Policy

The decision regarding distribution of earnings to its shareholders of a company related to number of factors. Many considerations may affect a firm's decision about its dividends, some of them are unique to that company and some of the more general considerations ate given subsequently.

a) Legal Rules

Certain legal rules may limit the amount of dividends a firm may pay. These legal constraints fall ino two categories. First, statutory may prevent a company from paying dividends. While specific limitations vary by state generally a corporation may not pay a dividend (i)if the firm's liabilities exceed its assets (ii)if the amount of the dividend exceeds the accumulated profits(retained earning), and (iii)if the dividend is being paid fro capital invested in the firm. The second type of legal restriction is unique to each firm and results from restrictions I debt and preferred stock contrasts.

b) Desire of Shareholders

Shareholders may be interested either in dividend incomes or capital gains. Wealthy shareholder in a high income tax bracket may be interested in capital gains as against current dividends. A retired and old person, whose source of income is dividend, would like to get regular dividend.

In a closely held company, management usually knows the desires of shareholders. So, they can easily adopt a dividend policy that satisfies all shareholders.. but ina widely held company, number of shares is very large and they have diverse desires regarding dividends and capital gains. Some shareholders want cash dividends, while other prefers bonus share.

c) Liquidity Position

Liquidity position or the cash availability of a company is another one of the major constraints in making dividend decision. The firm must have adequate cash while paying the dividend. The dividend payment means cash outflow. So the availability of cash of a

firm is important consideration for dividend payment. The greater the cash position and overall liquidity of a company, the greater is its ability to pay dividend regularly. While an immature firm faces difficulties in maintaining a sound cash liquidity position because of the expansion of the business, but a mature company generally have adequate liquidity and able to pay large amount of dividend with a sound cash position.

d) Access to the Capital Market

If a company can raises debt or equity in the capital market, it can pay dividend even the cash position of the firm is insufficient. A firm, which is large and well established and has a record of profitability and stability of earning, will not find much difficulty in raising funds in the capital market. Even if the firm is not in liquid position its ability to pay dividend will be higher because of its ability to raise funds in capital market. In contrast a small and new firm is riskier for potential investors so its ability to raise equity or debt funds from capital market is restricted. That's why small firms must retain more earnings to finance its investment opportunities. Thus a well established firm has higher dividend payout ratio than of a new and smaller one.

e) Control

If the company pays access cash dividend, there would be shortage of fund to finance investment opportunities, which must be fulfilled by issuing new securities. This affects the control position of existing shareholders. So, they are not desirable to distribute earning as dividend which prevents them to loose the control position of the company. The objective of maintaining control over the company by the existing management group or the body of the shareholders can be an important variable in influencing the company's dividend policy (Pandey: 1999).

f) Investment Opportunity

The dividend policy is greatly influenced by the financial need of the company. Companies invest its earning to the projects rather paying dividend, if any profitable project is found. "A growing firm gives precedence to the retention of earning over the payment of dividend in order to finance its expanding activities. But when the investment opportunities do not occur continuously but infrequently then the company may not

justify in retaining the earning at least during those period when such opportunities does not exists." (Pandey: 1999) When the investment opportunities occur in frequently, company follows a policy of paying dividend and raises external funds when the investment opportunities occur.

g)Tax Position of Shareholders

The tax position of stockholders also affects dividend policy. Corporation owned by largely taxpayers in high income tax brackets tend toward lower dividend payout where as corporations owned by small investors tend toward higher dividend payout..

h) Liquidity Position

The cash/bank balance of the firm influences its ability to pay dividends. A firm may have sufficient retained earnings, but if they are invested in fixed assets, cash may not be available to make dividend payment. Thus, the company must have adequate cash available as well as retained earning to pay dividends

i) Inflation

Inflation act as one of the constraint in the dividend policy. Cost of replacing assets increase due to inflation and funds generated by depreciation would be inadequate to replace the assets. To maintain the capital in act and preserve the earning power of the firm, earning would be retained. In another words, to maintain the capital in act that reduces dividend payment, the greater profit retention would be required.

j) Stability of Earning

A company can declare its dividend only when there is stability in its earning. Stable earning can predict the company's approximation regarding future earnings. The company with stable earning can pay out higher percent of earning as dividend than a firm with fluctuating earnings. A lower dividend will be easier to sustain if a firm is not certain that in succeeding years the anticipated earnings will be realized. In another words, if the earning is unstable, the company has to retain higher percentage of earning.

k) Restriction in Loan Agreement.

When the firm is experiencing liquidity, restriction on dividend payment may be employed by the lenders to protect their interests. This could be happen in those circumstances when a firm aggresses as a part of contract with its lenders that it will restrict dividend payment to conserve the company's ability to service debt. Similarly preferred stock agreements generally state that no cash dividends can be paid on the common stock until all accrued preferred dividend have been paid. In the period of these restrictions, the firm is forced to retain earning and have a low payout of dividend.

l) Tax position of Stockholders

The dividend payment of a company is highly influenced by the tax position of its owners. If a company is closely held by few taxpayers in high income tax brackets then they will certainly like to get the return of their investment in the form of capital gains rather than as dividends, which are subject to higher personal income tax rates. On the other hand, a high dividend payout might be preferred by the stockholders of a large widely held corporation.

2.5 Related Empirical Studies on Dividend Policy

Various studies have been made concerning the dividends and stock prices. Some of the major international studies on the relating to dividend are stated as below.

Friend and Puckett's Study

Friend and Puckett made a detailed study of 110 firms from 5 Industries during the year of 1956 to 1958. Their study was mainly focused on the relationship between stock price and dividend by the application of regression analysis. These five sample industries were form chemicals (n=20), electric utilities (n=25), electronic (n=20), food (n=25) and steels (n=20) sectors. Those industries wire selected to permit a distinction to be made between the results for the growth and non-growth industries and to provide a basic for comparison with results by other authors for earlier years. Both cyclical and non-cyclical industries were covered. The periods covered include a boom year for the economy when

stock prices leveled off after a substantial rise (1956) and s somewhat depressed year for the economy when stock prices, however rose strongly (1958).

They used dividend, retained earning, and price earning ratio as independent variable in their regression model of price function and dividend model acts the role of supply function. In dividend function, earning, last year's dividend and price earning ratio are independent variable. Symbolically, the price function and dividend supply function can be written as follows:

Price Function

$P1 = a + bD_t + cR_t + n(E/P)_{t-1}$

Where,

P_t = Price per share at time't'

D_t = Dividends at time't'

R_t = Retained earning at time't'

$E/P)_{t-1}$ = Lagged Earning Price Ratio

Dividend supply Function

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

Where,

E_t = Earning per share at time't'

D_{t-1} = Last years dividend

The followings are some basic assumptions of their study.

- Price doesn't contain the speculative components
- Earning fluctuation may not sum zero over the sample
- Dividend reacts year- to- year fluctuation in earnings.

The regression equation of five industries was based on the equation of

P1 = a + bD1+ cR1 presents the usual simple linear relationship between average prices and dividend and retained earnings to show with the data. They found the customary strong dividend and relatively weak retained earnings effect in three of five industries i.e., chemicals, foods and steels.

Again they tested other regression equation by adding lagged earning price ratio to the earlier equation results the following equation,

$P_t = a + bD_1 + cR_1 + d(E/P)_{t+1}$

After testing this equation, they found the result that more than 80% of the variation in stock price can be explained by three independent variables. Dividends have a predominant influence of stock price in the three industries among five but they found the differences between the dividends and retained earning coefficients were not quite so marked as in the first set of regression. The dividend and retained earning are closer to each other for all the industries in both year except for steel in 1956, and the correlation are higher, again except for steels.

The study also shows the calculation of dividend supply equation in the form of $D_t = e + fE_t + gD_{t-1}$ h $(E/P)_{t-1}$ and derived price equation for four industry group in 1958. Their derive price equation shows no significant changes from those obtained from the single equation approach as explained above. They argued that the stock price, or more accurately the price earning ratio, does not seem to have significant effect on dividend payout. On the other hand, they noted that the retained earning effect is increased relatively in the three of four cases tested. Furthermore, they argued that their result suggested that price effects on dividend supply are probably not a serious source of bias in the customary derivation of dividend and retained earnings effects on stock prices, though such a bias might be marked if the distributing effects of short run income movements are sufficiently great.

Similarly they tested the regression equation of $P_1 = a + bD_1 + cR_1 + d(E/P)_{t-1}$ by using normalized earnings again. They obtained normalized retained earnings by subtracting

dividends from normalized earnings. That normalization procedure was based on the period 1950-1961. Again they added prior year's normalized earning price variable and they compared the result. Comparing the result, they found that there was significant role of normalized earning and retained earning but effect of normalized price earning ratio was constant. When they examined later equation, they found that the difference between dividend and retained earning coefficient disappeared. Finally, they concluded that management might be able to increase prices somewhat by raising dividend in food and steel industries.

The conclusion of their study was that the management might be able, at least in some measure to increase in stock price in no growth industries by raising dividends and in growth industries by paying low dividends.

Linter's Study

John Linter made an important study in 1956 on 'Distribution of Incomes of corporations among Dividend, Retained earning and taxes', focusing on the behavioral aspect of dividend policy in American context. He investigated a partial adjustment model as he tested the dividend pattern of 28 companies According to him; dividend is a function of earnings of that year, existing dividend rate, target payout ratio and speed of adjustment.

The following were the basic objectives of the study:

1) To identify occasion when a change in dividends might well have under active consideration even though no change was made
2) To determine the factors which existed most actively into dividends.

His study reflects that a major portion of dividend of a firm could be expressed in the following ways:

$$DIV^*_t = P\ (EPS_t) \qquad \text{----------(1)}$$

And $DIV_t - DIV_{t-1} = a + b\ (DIV^*_t - DIV_{t-1}) + e_t$ --------(2)

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

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

Where,

DIV*t = Firm's desired payment

e_t = Error term

p = targeted payout ratio

a = constant relating to dividend growth

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

The major findings of this study were as follows:

- Firms generally think in terms of proportion of earning to be paid out.
- Investments required are not considered for modifying the pattern of dividend behavior.
- Firms generally have targeted payout ratios in view while determining change in dividend rate or dividend per share.

Van Horne and McDonald's Study

Van Horne and McDonald conducted comprehensive study on dividend policy and new equity financing. The purpose of this study was to investigate the combined effect of dividend policy and new equity financing decision on the market value of the firm's common stocks.

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

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

The first model was,

$P_0/E_0 = a_0 + a_1(g) + a_2 (D_0/E_0) + a_3 (Lev) + u$

Where,

P_0/E_0 = Closing market price in 1968 divided by average EPS for 1967 & 1968.

g = Expected growth rate, measured by the compound annual rate of growth in assets per share for 1960 through 1968

D_0/E_0 = Dividend payout, measured by cash dividend in 1968 divided by earnings in 1968.

Lev = Financial risk, measured by interest charges divided by the difference of operating revenues and operating expenses.

u = Error term.

The Second Model was,

$P_0/E_0 = a_0 + a_1(g) + a_2(D_0/E_0) + a_3(Lev) + a_4(F_a) + a_5(F_b) + a_6(F_c) + a_7(F_d) + u$

Where,

F_a, F_b, F_c and F_d are dummy variables corresponding to "new issue ratio" (NIR) groups A through D

It is noted that they had grouped the firms in five categories A, B, C, D and E by NIR. For each firm the value of dummy variables representing its NIR group is one and the value of remaining dummy variables is zero.

Again, they tested the following regression equation for electronics electronic components industry.

$P_0/E_0 = a_0 + a_1(g) + a_2(D_0/E_0) + a_3(Lev) + a_4(OR) + u$

Where,

Lev = Financial risk, measured by long term debt plus preferred stock divided by net worth as of the end of 1968.

OR = Operating risk. Measured by the standard error for the regression of Operating earnings per share on time for 198601 through 1968, and rest are as in First Model above.

By using these models, they compared the result obtained for the firms which both pay dividend and engage in new equity financing with other firms in an industry sample. They concluded that for electric utility firms in 1968, share value was not adversely affected by new equity financing in the presence of cash dividends, except for those firms in the highest new issue group and it made new equity a more costly form of financing that the retention for earnings. They also indicated that the payment of dividend through excessive component industry, a significant relationship between new equity financing and value was not demonstrated.

Deepak Chawla and G. Shrinivasan's Study

They studied the impact of dividend and retention on share price. The followings were the prime objectives of their study.

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

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

1 Price Fuction

$P_1 = f [D_t, R_t, (P/E)^1 _{(t-1)}]$

Dividend Supply Function,

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

2 Identity

$E_t = D_t + R_{ts}$

Where,

P = Market price per share

D = Dividend per share.

R = Retained earning per share.

E = Earning per share.

$(P/E)^1$ = Deviation from the sample, average of price earning's ratio.

T = Subscript for time.

As per the financial theories they expected the coefficients of both dividend and retained earnings to be positive in the price equation. Similarly in the dividend supply function also they expected a positive sign for current earnings and previous dividend.

They selected 18 chemicals and 13 sugar companies and estimated cross-sectional relationship for the years 1969 and 1973. They collected the required data from the official directory of Bombay Stock Exchange. They used two stages least square technique for estimation .They also used lagged, earnings price ratio instead of lagged price earnings ratio. i.e $P/E_{(t-1).}$

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

very high as compared to retained earnings for chemical industry. They also found that coefficient of dividend was significant ant one percent level in both years whereas coefficient so retained earnings was significant at ten percent level in 1969 and one percent level in 1973.

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

Shlomo Benartzi, Roni Michaely and Richard Thalm's Study

Shlomo Benartzi, Roni Michaely and Richard Thalm conducted a research on 'Do Change in Dividends Signals the Future or the Past' in 1997. They collected the data from two years during the period 1989-1991 from listed companies in American Stock Exchange. They analyzed the data by using different statistical tools and arrive at conclusion that:

Why do firms pay dividend even after knowing to pay dividend is costly in various ways? The reactions of market towards changing dividends are good, more is better. Dividend provides information to the market changes in dividends as signals something about the present: The current increase in earning is permanent.

It implies that the stock price and dividend are independent variables. They found negative sign in Sugar Factory for both the years. They left the Sugar Factory for further analysis. By analyzing the data of Chemical Industries they found coefficient of dividend was very high as compare to retained earnings. They arrived at conclusion that dividend hypothesis holds well in Chemical Industry. They emphasized that impact of dividend is more pronounced than that of retained earnings but the market was started shifting towards more weigh for retained earnings.

2.6 Empirical Nepalese Studies on Dividend Policy

The review of studies regarding dividend policy can be broadly classified into two categories.

a) Bishnu Hari Bhattarai's Study

The study of the dividend decision and its impact on the stock valuation was carried out by Bishnu Hari Bhattarai, in 19996 using 10 companies of various sectors. The basic objective of the study was to identify the relationship between dividend and the stock price. The major objectives of this study can be stated as follows:

i. Highlight various aspects of dividend policies and practices in Nepal.
ii. Analyze the variables such as profit, dividend, retained earning, growth rate and relevant variables to how the relationship between the value and other ingredients affecting it.
iii. Provide feedback to the policy makers and executive working in various companies chosen for study based on the findings of the analysis.

The major findings of this study are as follows:

i. The companies while paying dividend generally neglect shareholder's expectations.
ii. Dividends were paid out in profitable years.
iii. In aggregate, there was no stable dividend paid by the companies i.e. instability of dividend.
iv. There were no criteria to adopt a certain payout ratio. There is haphazard payout ratio in the companies under study.
v. Cash balance and dividend payment were positively correlated.
vi. Mostly the joint venture companies were paying dividend.
vii. There was positive impact of dividend on valuation of shares.
viii. Dividend paid was inadequate to cover the required rate of return of the investors.
ix. Market price considerably higher than actual net worth.

b) Navaraj Adhikari's Study

The study has covered the period from 1990 to 1996 with total observations of 47 in financial sector and 30 non-financial sectors. This study has used both primary and secondary data. The major objectives of this study were to assess corporate dividend practices in Nepal. The specific objectives were as follows:

i. To analyze the properties of portfolios formed on dividends.
ii. To examine the relationship between dividends & stock prices.
iii. To survey the opinions of financial executives on corporate dividend practices.

The major conclusions, of this research study were as follows:

It is observed that there are differences in financial position of high dividend paying and low dividend paying companies. Other things remaining the same, financial position of high dividend paying companies is comparatively better than that of low dividend paying companies. Thus 'Dividends affect the market price of share' is the major conclusion of this study.

Likewise, the other findings based on primary data are given below:

i. The price of common stock was induced by dividend payout ratio.
ii. Nepalese shareholders were not really indifferent towards payments or non-payment of dividend.
iii. The majority of the respondents feel that the major motives to pay cash dividend was to convey information to shareholders that the company is in good position.
iv. As regards dividend as a residual decision, the majority of the respondents feel that it was not a residual decision.

With respect to factors affecting corporate dividend policy, the majority of the respondents gave the first priority to 'earnings' the second priority to 'availability of cash ' , the third priority to 'past dividends' & fourth priority to 'concern about maintaining or increasing stock price'.

c) Anjani Raj Bhattarai's Study

Anjani Raj Bhattarai conducted his study on 'Share market in Nepal' in 1990. His study has following issues related to dividend practices:

- The actual percentage dividend was not matching with the expected percentage dividend. So must of the listed companies declaring less percentage than risk free rate of return and risk premium are unable to maintain investors psychology in marketing.
- Most of the companies are paying less than the expected cash dividend per share to its investors. Most companies were underwriting the expectation of the investors and there by resulting the two marketability o shares on trading floor of stock exchange.
- There was a huge gap in the percentage of cash dividend paid by the public companies.
- There were mismatch between calculated and quoted price of share observed only one calculated price of share was near the actual Market price of the share. This reveals over pricing were guided by technical factors.
- The price-earning ratio showing by most of the company is lower.

Bhattarai's study couldn't be untouched from limitations but his topic was only focuses on dividend policy. So discussion on those limitations might be irrelevant here.

d) Rishi Raj Gautam's study

Rishi Raj Gautam has conducted a study on dividend policy in commercial banks a comparative study of NGBL, NIBL and NABIL in 1995. His study reveals some important aspects of dividend performance of three samples. Major finding of his studies are as follows:

- Commercial banks represent a robust body of profit earning organization in comparing with other sectors.
- Though they have good earning potentials, it doesn't seem that commercial banks are guided by clearly defined dividend policy.

- Share of the financial institution are actively traded and market price are increasing.
- Average EPS and DPS of the concerned banks are satisfactory.
- This study indicates there are the largest fluctuation in EPS and DPS, on the other hand, have relatively more consistency DPS in all samples.
- One of the important finding of this study is that none of the sample has defined the dividend strategy. On the other hand there was significant relationship percentage between earning and dividend of expansion program.

However Gautam's study suffers from following limitations:

There are many factors affects dividend policy, those factors are DPS, DPS, MVPS, DPR, dividend yield, liquidity ratio and profitability ratio. But only has used a few financial indicators that result the validity of the research is not worthwhile.

In this study, he has selected samples from commercial bank only. It would be perfect research if he has taken the samples from other sectors and performs while spread analysis in the variables mentioned above.

e) N.P. Khatiwada's Study

N.P. Khatiwada has conducted a study on 'Impact of dividend and earning announcement on shareholder's return and stock prices in Nepal' in May 2001, through the data collected from 053/54 to 055/56 for four joint venture banks viz. Nepal Indosuez Bank Ltd., Nepal SBI Bank Ltd., Nepal Grindlays Bank Ltd. and Nepal Bangladesh Bank Limited.

The main objectives of the study were as follows:

- To analyze the impact of earning and dividend announcement on shareholder's return.
- To see the correlation between the return of the individual securities with market return.
- To identify the quality of systematic and unsystematic system.

Major findings of the study are as follows:

- Announcement of dividend and earning didn't affect the shareholders return in average.
- Other banks except Nepal SBI Bank Ltd. having different dividend rates didn't provide significant abnormal return to the shareholders.
- Shareholders realized the positive abnormal return from NB Bank, SBI Bank and Grindlays Bank.

f) Y.B. Katawal's Study

Y.B. Katawal has conducted a research on 'A comparative study of dividend policy in commercial banks' in July 2001, based on data collected from 1994/95 to 19998/99 for six commercial banks.

He has conducted the research with following objectives:

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

The major findings of this study are as follows:

- Average EPS and DPS for the period covered by the study of all the concerned banks are satisfactory.
- Analysis of CV indicated that there is largest fluctuation in EPS and DPS and other are relatively more consistent.
- The analysis of DPR shows that none of the sample banks has consistent dividend policy.
- The market value of shares in market is fluctuating in all sample banks.
- The most important decision is that no specific dividend payment strategies are following by these banks. Payment of cash dividend and stock dividend are made

without wise managerial decision due to unstable and adequate dividend and unequal payout ratio.

2.7 Review of Articles

To facilitate the study following articles are review under this study

I) International Journals and Articles

R. Mehotra's Study

Rohit Mehotra (2003) conducted a study on 'Dividend Policy and its Effect on Market Pricing', the study is concerned with dividend and its effect on the price fluctuation of the stock. This study is based on the scenario of Indian stock market, top 50 Indian companies of Bombay stock exchange has been taken as sample of this study. All the samples are paying dividend, although some of the samples suffering from losses, they are also paying nominal dividend using their prior reserves.

His study reveals that market risk of any security depends on its beta (b), which shows the relationship between the sensex return and security return. It also measures the relative risk associated with the security with respect to market. Higher the beta, greater the risk associated with the security. If the value of beta is less than one, he security will affected lesser than the proportion of the market sensex.

This research reflects that some of the renowned companies followed the conservation policy while others were paying an excellent dividend. Samples representing the companies like NIIT, Satyam Computers, Glaxo, P &G, Health care, etc., 37% of the sample sizes have performed as per the SENSEX movement. All of these companies have very good track record of dividend payment and appreciated by investors. But, since April 2000, Indian stock market is being victim of continuous chain of national and international negative sentimental (including the US slowdown to TEHELEKA issue), due to which the share price has come down drastically.

Samples holding 26% of the total samples, including Hindustan Lever Limited, ITC, Reliance India Ltd. performed extraordinarily well after debacle of SENSEX. The stock

of these companies are continuously paying handsome dividend and showing positive trend in the price movement and have never experienced significant downfall in past couple of years.

Due to some specific factors, 25% of the samples having fluctuation in dividend payment from last couple of years. Though factors may consist of liberalized economic policy, strict government policy in certain sectors, economic fluctuations etc. Some samples are continuously paying certain amount of the dividend from last couple of years, a continuous dividend payment record find no appreciation along with this, they want smooth performance of the company so that they can earn some capital gain also.

Rest of companies, representing 11% of the sample size performed negatively. Those companies were paying dividend on regular basis, the stock price were declining continuously from last couple of years. This situation reveals that investors are very rational about their current as well as future earning. They can't accept any window dressing.

In conclusion, investors make equity investment with the expectation of capital gains irrespective of whether they are short term or long term investors. Typically there is who can ensure capital gains to investors without declaring continuous dividend. In other words, the investors do care about dividends however a small impact on their wealth. It is not only the investors care about dividend but also growth in dividend and profitability of the companies in which they made investments. Since the dividends are taxed in the hands of the companies, but not investors, Indian investors don't give weightage on tax matter unlike US market where tax is the major determinants for the investors for accepting dividends.

Oaktree Research

A recent research on dividend was published on Oaktree (2003) a website relating to business and finance consist of a deep study on dividend with heading of 'Dividend: Relevance or reverence'. This study describes dividend as, dividend represents one of the most interesting puzzles in corporate finance, knowing that dividend are paid in the face of tax disadvantage. This study attempts to tell the answer of the following questions:

- Why do corporations continue to pay dividends?
- What then is the relevance of the dividends?
- What does it play the role in corporate finance?

This study wants to describe the role of dividend policy by two schools of thoughts in the view on whether the dividend adds to the value to the firm.
The first school of thoughts originated by Modigliani and Miller claims that dividend should have no impact on the value of the firm under the perfect market condition. The shareholders of the firm are indifferent towards retention of net income and payment of the dividend, since the dividend policy of a firm doesn't affect its current price.

In the second school of thought, the imperfect market school begins to relax the unrealistic assumption that Modigliani and Miller have introduced. They begin to introduce both dividend and capital gain taxes. If dividends are taxed at a different rate of capital gain, a distinct preference could develop for either dividend income or capital gains. In 1979, Elton and Gruber found evidence that is consistent with the notion that the investors prefer capital gain to dividend.

This study considers following factors:

Signaling effects of dividend

In 1984, Easterbrook studied the signaling effect of dividend and its role in reducing agency cost. He believed that firms that pay high dividend signals the managers intent to maximize investors wealth and to subject him to capital market monitoring and reduces the potential for managerial self dealing and thus reduces the agency cost. His study states that quality firms will signal their strength to investors by passing and sustainable dividend.

Dividend and corporate governance

Easterbook didn't state about motivation that will drive a firm to pay the dividend in his research. Investigation on this issue has derived the outcome models and substitute model. They formulated two hypotheses on the former model:

1. Economies with better investor protection will have higher dividends.
2. Economies with higher investors rights, firms with growth opportunities will retain earning and invest them, resulting in low dividend payout whereas mature firm will have low growth opportunities and will have high dividend payout ratios.

Hypothesis of second model is as follows:

1. Economies with weak investor protection will have higher dividends.
2. Firms with better growth prospects in weak investor protection economies will have higher dividend payout ratio than firms with lower growth opportunities

The study conducted by Faccio, Long and Young (2001) investigated the link between dividend and expropriation of minority shareholders. In their study, they found that loosely controlled firms and those with lower CV paid lower dividend. Efficient capital Markey requires firms to pay high dividend when agency problem are high. The findings of FLY study are as follows:

- Dividend work to constrain agency problem in Europe.
- Dividends do not work constrain agency problem in Asia.
- Capital structure works to constrain problem in Europe.
- Capital structure facilitates agency problem in Asia through cross shareholding and pyramids.

This study was conducted with that companies paying higher dividend had strong operating track records and growing profits.

A.K. Saxena's Study

A study conducted by A.K. Saxena (2003) conducted a study entitled 'Determinants of dividend policy: Regulated vs unregulated firms', where he tries to state the importance of dividend policy in several reasons for example, using dividend as a mechanism for the financial signaling to the outsiders regarding growth and stability of the firm, the role of dividend in capital structure, the dividend decision is key phenomenon in establishment of investment decisions.

Though there are sufficient literatures in dividend policy, most of the study excludes regulated firm from their analysis. His study includes several financial variables to explain the possible differences in the dividend policy of both regulated and unregulated firms. While comparing regulated and unregulated firms, the study reflects one interesting results. On average the regulated firms are less risky, has a lower growth rate, has such fewer insiders holding its common stocks, and has fewer investment opportunities, but pays higher percentage in dividend.

His study consists of the data randomly drawn from 333 firms. The total sample is split between 235 unregulated and 98 regulated firms, covering 56 industries. The regulated samples are taken from commercial banking, saving and loan association, investment and brokerage services, life and prosperity and causality insurance, electric utilities, gas, petroleum, telecommunications, railroads, and airlines industries.

The study applied regression equation and hypothesis in order to predict the relationship of variables (with respect o dividend payout ratio) for regulated and unregulated firms.

The study also reflects that the mean dividend payout for regulated firm is significantly larger than that for unregulated firms. Unregulated firms grew more than regulated ones in the samples over past years. This probably states the fact that regulated firms are more matured and have stabilized over times. It might indicate the fact that managers of regulated firms don't have as much freedom to make them grew as their counterparts in unregulated firms.

This model predicts that dividend payout of unregulated firms are inversely related to past and expected growth, their systematic risk, and the level of holding of common stocks by the managers, directors and officers. On the other hand, payouts are directly related to the number of stockholders in unregulated firms. While the results for the regulated subgroup provide some interesting insights regarding the payout behavior of regulated firms. It seems that insiders don't play a significant role in dividend policy of regulated firms. It is suggested that if a firm is unregulated, the firm's insiders will act to 'regulate' and monitor the firm's financial performance in long run. They do not care as

much about receiving dividend today, if they can reinvest these dollars in positive net value projects that will increase firm's value, which in turn attract new investors.

The conclusion of this study reflects that a firm's dividend policy will depend upon its past growth rate, future growth rate and systematic risk, the percentage of common stock held by insiders and the number of common stock holders. More importantly, however some of the determinants of dividend policy are different for regulated and unregulated firms. Specially, the percentage of common stock held by insiders, and expected future growth rate, do not play a key role in regulated firm's payout rat

ii) Review of Articles in Nepalese Perspective

Very few articles relating directly or indirectly with dividend and stock price are published in Nepal. Some of them, which are significant in this study, are reviewed in this section.

Manohar Krishna Shrestha's Study

Dr. Manohar Krishna Shrestha published an article in 1981 entitled "Public Enterprises have Dividend Paying Ability?" In his article he emphasized that public enterprises are neither positive to pay dividend nor self-supporting in financial matters due to interference in day-to-day affairs by government. HMG/N appoints high-ranking officials. They do nothing but showing their bureaucratic behavior and they are the enemy of efficiency and lead the corporation to face losses. He points out that HMG wants to tap resources through dividend, following criteria should be followed:

Proper evaluation of public enterprises on capability of paying dividend through corporate co-ordination committee. Imposition of fixed rate dividend policy by government to financially sound public enterprises. Circulating the information to all public enterprises about the minimum rate of dividend. Identification of objectives in Corporation Act, Company Act so as to clarify public enterprises regarding their financial obligation to pay dividend to HMG.

In another study "Dividend Policy in selected public enterprises", he has discussed about streamline dividend policy. He collected data of 18 public limited companies for the year

1982-83. He analyzed the data by using different models and concluded that dividend policy constitutes one of the most critical issues of the public limited companies. Many of public limited companies are found to pay negligible dividend to the shareholders in whom HMG/N proved to be potential investors. Many factors affect the payment depending upon investors' need and preferences on the one hand and the financing need of the public limited companies to the potential investment opportunities on the other hand. Dividend policy involves many aspects such as selecting the types of dividend to be paid either cash or stock and other forms as well as determining stable or fluctuating or minimum plus extra dividend payment. The application of Walter's and Gordon's dividend models in calculating the stock value of selected public limited companies reveal both acceptance and fantastic results.

Dr. R.S. Pradhan's Study

Dr. R.S. Pradhan has conducted a study on small Market Behavior in **A Small Capital Market: A case of Nepal** in 1993. It is pertinent to put forth here because he has analyzed various ratios related to dividend and market price of shares. The study was based on the pooled – cross sectional data of 17 enterprises covering the year from 1986 to 1990.

The objectives of this study were as follows:

i. To assess the stock market behavior in Nepal.

ii. To examine the relationship of market equity, market value to book value, price earning, and dividends with liquidity, profitability, leverage, assets turnover, and interest coverage.

The following model was employed.

$V = b_0 + b_1 LIQ + b_2 LEV + b_3 EARN + b_4 TURN + b_5 COV + Ui$…..

The dependent variable, V chosen for the study has been are specified as under:

-Market equity, number of shares multiplied by market price of shares (ME).
-Market value of equity to its book value (MV/BV)
-Price –earning ratio (PE)

-Dividend per share to market price per share (DPS/MPS)

-Dividend per share to earning per share (DPS /EPS)

The independent variables are specified as:

LIQ = Current Ratio (CR) to Quick / Acid Test Ratio (QR)

LEV = Long –Term Debt to Total Assets(LTD /TA) or Long-Term Debt to Total Capitalization (LTD /TC). Total Capitalization is specified as Long-Term Debt plus Net Worth.

EARN = return on Assets, i.e. Earnings Before Tax to Total Assets (ROA) or Return on Net Worth, i.e. Earnings Before Tax to Net Worth (RONW).

COV = Interest Coverage Ratio, i.e. Earnings Before Tax to Interest.

TURN = Fixed Assets Turnover, i.e. Sales to Average Fixed Assets (S/FA), or Total Assets Turnover, i.e. Sales to Average Total Assets (S/ TA)

U = Error Term

Some findings of his study, among others were as follows:

i. Stocks with larger ratio of dividend per share to market price per share have higher liquidity. Liquidity position of stocks paying lower dividends is also more inconsistent as compared to stocks paying higher dividends.
ii. Stocks with larger ratio of dividend per share to market price per share have lower leverage ratios. So, leverage ratios of stocks paying smaller dividends were also more variable as compared to stocks paying higher dividends.
iii. Stocks with larger ratio of dividend per share to market price per share also have higher earnings. But these earning ratios of stocks paying larger dividends were also more variable as compared to stocks paying smaller dividends.
iv. Positive relationship is observed between the ratio of dividend per share to market price per share and turnover ratios. Stocks with larger ratio of dividend per share to market price per share also have higher turnover ratios. Turnover ratios of stocks

paying larger dividends are also more variable than that of stocks paying smaller dividends.

v. There is also a positive relationship between the ratio of dividend per share to a market price per share and interest coverage. Stocks with higher ratio of dividend per share to market price per share also have higher interest coverage. Interest coverage of stocks paying larger dividends were also more variable as compared to stocks paying smaller dividends.

vi. So, in conclusion, it indicates positive relationship of dividend per share to market price per share with liquidity, profitability, assets turnover and interest coverage; and negative relationship with leverage.

Dr. M.K. Shrestha's Article

Dr. M.K. Shrestha has written an article about "**Public Enterprises; Have They Dividend Paying Ability?"** which was published in the book 'PRASHASAN' in March 1981. It gives short glimpse of the dividend performance of some public enterprises of that time in Nepal. Dr. Shrestha has highlighted (focused) the following issues in the article.

Government of Nepal wants two things from the public enterprises: (i) they should be in a position to pay minimum dividend & (ii) Public enterprises should be self-supporting in financial matters in future years to come.

But these both objectives are not achieved by public enterprises.

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

2. Another reason of this is the lack of self-criticism and self-consciousness. Esman[33] has pointed out that lack of favorable leadership is one of the biggest constraints to institution building. Moreover corporate leadership comes, as managers are not ready to have self-criticisms. In fact, all so called managers of corporations have not been able to identify themselves regarding what they can contribute as managers of corporations. So Government of Nepal must be in a position to develop a financial target on corporate investment by imposing financial obligation on corporations.
3. The articles points out the irony of government biasness that government has not allowed banks to adopt an independent dividend policy and Government of Nepal is found to have pressurized on dividend payment in case of Nepal Bank Limited regardless of profit. But, it has allowed Rastriya Banijya Bank to be relieved from dividend obligation despite considerable profit.
4. The improvement suggested by authors are:
   i. Adopt a criteria-guided policy to drain resources from corporations through the medium of dividend payment.
   ii. Realization by managers about cost of equity capital and dividend obligation.

   If Government of Nepal wants to tap resources through dividend, the following criteria should be followed. Proper evaluation of public enterprises interns of capabilities of paying dividend through corporation coordination committee.

   i. Imposition of fixed rate of dividend by government on financially sound public enterprises.
   ii. Circulating the information about minimum rate of dividend to all public enterprises.
   iii. Specifying performance targets in terms of profit, priorities on timings and plans and development of strategic plans that bridges the gap between aspiration and reality.

   Identification of corporation objectives in Corporations Act, Company Act or special charters so as to clarify public enterprise mangers regarding their financial obligation to pay dividend to Government of Nepal.

2.8 Concluding Remark

There are many reasons for paying higher dividend and there are many reasons for not paying higher dividend. As a result, dividend policies have been controversial. Dividend policy decides about the division of earnings between dividend payout and retained earnings. When the bank retains its earning, it will result decreasing leverage ratio and increasing profit. But when the bank does not have reinvestment opportunity or expected rate of return of that opportunity is less than risk free rate, it decreases EPS and market price of share. In such situation, dividend payment to shareholders is taken as the best because shareholders might have investment opportunities to invest elsewhere. When the bank pays dividend the cash balance, reserve amount as well as total assets and net worth of the bank decreases and the market price also drop. If the bank pays higher dividend, it may need to raise capital through capital market that reduces ownership control of existing shareholders. In another way to raise capital through debenture or new issue, which ultimately affects the risk of the firm. Therefore, a wise policy should be maintained between shareholders interest and corporate growth from internally generated funds.

Dividend serves as a simple tool of management interpretation of the firm's recent performance and its future prospects. It is considered that dividend policy should be concerned with the well being of the shareholder, which can be partial measured by dividend received but more accurately measured in terms of the market value of the stock. Dividend can be distributed in various forms like regular dividend, cash dividend, interim dividend, stock dividend scrip dividend bond dividend etc. Commercial banks have been carrying out the practice of dividend policy as provision mentioned in Nepal company act 1997(Endi Consultant Research Group: 1997:P.43).The decision regarding dividend policy are affected by number of constraint like legal rule, desire of shareholders liquidity position access to the market, control, investment opportunity , tax position if shareholders etc.

M & M argues that declaration of dividend does not affect the market price. The value of a firm depends on its earnings it depends on its investment policy. Thus, when the investment decision is given, the dividend decision cannot affect the value of the firm. In

a perfect market, a firm may face one of the following two situations regarding the payment of dividends. So this theory is known as dividend irrelevance theory. But the bird-in-the-hand theory, however, states that dividends are relevant. Remember that total return (k) is equal to dividend yield plus capital gains. Myron Gordon and John Linter took this equation and assumed that k would decrease as a company's payout increased. As such, as a company increases its payout ratio, investors become concerned that the company's future capital gains will dissipate since the retained earnings that the company reinvests in to the business will be less. Gordon and Lintner argued that investors value dividends more than capital gains when making decisions related to stocks. In this theory "the bird in the hand' is referring to dividends and "the bush" is referring to capital gains.

2.3 Research Gap

From the above in depth study, it can be concluded that dividend policy is one of the key success for the organization. Dividend policy is the vital factor of the successful organization that enables company to achieve their goal and shareholders satisfaction. Hence it is accepted as the nerve (courage) centre for any type of organization. The previous research studies reviewed are related to dividend policy of selected banks, which make clear that no studies have been conducted specifically on Dividend policy of these five banks. Here there exists a research gap between the present and past research. This research is conducted to fill up this research gap. Particularly in five different banks it has been found that generally researcher is interested in the historical data, only that absolute the focusing objectives of the research. The findings were not tested on the practical grounds. Similarly the financial strengths and the current situation of the banks have been drastically different from the recent times.

At present many changes have been taken in our country. There has been drastic change in the economical as well as political situation of the country and has followed the policy of liberalization, privatization and globalization. As a result every business organization is also affected. Many more companies have been established after the change. The previous studies on this topic may not coordinate with the present scenario. Therefore it is necessary to bring out new fresh study on dividend policy of selected five commercial

joint venture banks to suggest the possible ways for the improvement of the sector. Thus to fulfill this gap between previous and present scenario, this research has been conducted.

CAPTER III

RESEARCH METHOLOGY

3.1 Introduction

Research methodology is a way to study systematically to solve the research problem *(Kothari: 1990).* The basic objective of the study is to analyze the dividend policy and practices of Nepalese Commercial Banks and the factors that affect it. It also tries study existing EPS, DPS, Payout Ratio, MPPS, P/E ratio, EY and DY of samples banks of Commercial Banks taken as sample for data analysis purpose. It is given in another subtopic of this section. Basically secondary data will be used for analysis.

3.2 Research Design

Research design is a plan, structure and strategy of investigation. It is conceived so as to obtain answers to research questions and to control variance. Research design helps in the analysis of data related to the study topic. It is a controlling media for the collection of data. It helps to collect the accurate information, which is related to dividend practices of the commercial Banks. The research design of this study will be descriptive as well as analytical by using the all variables related to the dividend policy of commercial Banks. For the analytical purpose, the reports of related Commercial Banks will be collected from the year 2002/03 to 2008/2009.

3.3 Populations and Sample

Since mid 1980s when Nepal government adopted economic liberalization policy in Nepal many commercial banks have been established within a short period of time. There are many commercial Banks whose share is traded actively in the stock market. It is not possible to study all of them regarding the study topic. Therefore sampling technique will be used for selecting sample from population.

Out of 30 listed commercial banks in Nepal, this research work has selected 5

Commercial Banks in sample for the study purpose. The samples selected for this study are as given below:

1. Nabil Bank Ltd (NABIL)
2. Nepal Investment Bank Ltd (NIBL)
3. Himalayan Bank Ltd (HBL)
4. Standard Chartered Bank Nepal Limited (SCBNL)
5. Everest Bank Limited (EBL)

In this research study, the sample size is 16.66% of the population size.

3.4 Nature and Sources of Data

The study mainly conducted on the basis of secondary data. The secondary data has been collected from annual reports of concerned commercial banks. Other supplementary data and information are obtained from Nepal Rastra Bank's Reports. In addition to it, the other data are collected from Financial Statement published by Nepal Stock Exchanged Ltd., Ministry of Finance SEBON and National Planning Commission.

3.5 Method of Analysis

The analysis of the commercial banks data will be conducted according to the pattern of data available. Various financial and statistical tools have been applied to analyze the variables regarding the study topic. The various calculated results have been obtained through financial and statistical tools. They are tabulated under different headings by using various financial and statistical tools.

3.5.1 Financial Tools

The following financial tools have been used in the study.

Earning Per Share (EPS)

Earning per share refers the rupee amount earned per share of common stock outstanding. It measures the profitability of the shareholders investment. The earning per share shows

the profitability of the banks and finance companies. The higher earning indicates the better achievements in terms of profitability of the banks by mobilizing their funds and vice-versa. In other words, the earning per share indicates the strength and weakness of the banks.

Earning per Share is computed to know the earning capacity and to make comparison between concerned commercial banks. This ratio can be computed by dividing the earning available to common shareholders by the total number of common shares outstanding. Thus,

$$EPS = \frac{Earning\ Available\ to\ Common\ Stockholders}{Number\ of\ Ordinary\ Outstanding}$$

Dividend Per Share (DPS)

Dividend per share indicates the rupee earnings distributed to common stockholders per share held by them. It measures the dividend distribution to each equity shareholders. Dividend per share shows the portion of earning distribution to the shareholders on per share basis. Generally, the higher DPS creates positive attitude of the shareholders toward the banks. Dividend per share helps to increase the market value to the share. It also works as the indicator for better performance of the bank management.

It is calculated by dividing the total dividend distributed to equity shareholder by the total number of equity shares outstanding. Thus,

$$DPS = \frac{Total\ \ Amount\ of\ Dividend\ Paid\ to\ Ordinary\ Shareholders}{Number\ of\ Ordinary\ Shares\ Outstanding}$$

Dividend Percent (DP)

Dividend percent is the ratio of dividend per share to the paid- up price per ordinary share. It can be calculated as:

$$DP = \frac{Dividend\ Per\ Share}{Paid - Up\ Price\ Per\ Share}$$

Dividend Payout Ratio (DPR)

It is the portion of earning paid in the form of dividend. This ratio shows what percentage of profit is distributed as dividend and what percentage is retained as reserve and surplus for the growth of the banks. The dividend payout ratio of the banks depends upon the earnings made by the banks. Higher earning enhances the ability to pay more dividend and vice-versa.

There is an inverse relationship between dividend and retained earning. The higher the dividend payout ratio, the lower will be the proportion of retained earning and vice versa. The capacity of internal financing of the firm is checked out by the retention ratio.

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

$$DPR = \frac{Dividend\ Per\ Share}{Earning\ Per\ Share}$$

And, Retention Ratio = (1-Dividend payout ratio)

= (1-DPR)

Price Earning Ratio (P/E Ratio)/ Earning Multiplier

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

The P/E ratio measures investor's expectation and market appraisal of the performance of the firm. The higher P/E ratio implies the high market share price of a stock. This ratio is computed by dividing earning per share to market price. Thus,

$$P/E = \frac{Market\ Price\ Per\ Share}{Earning\ Per\ Share}$$

Earning Yield (EY)

Earning yield is the percentage of earning per share to market price per share in the stock market. In other words, it is a financial ratio relating to earning per share to the market share price at a particular time. It measures the earning in relation to market value of the share. It gives some idea that of how much an investor is earning for his money. The share with higher earnings yield is worth buying. It is calculated as:

$$Earning\ Yield = \frac{Earning\ Per\ Share}{Market\ Price\ Per}$$

Dividend Yield (DY)

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

This ratio highly influences the market price per share because a small change in dividend per share can bring effective change in the market value of the share. The share with higher dividend yields is worth buying. Thus the price of higher dividend yields increases sharply in the market. Dividend has important guidance to commit funds for the buying the share in the secondary market. This ratio is calculated by dividing dividend per share by market price of the stock. Thus,

$$DY = \frac{Dividend\ Per\ Share}{Market\ Per\ Share}$$

3.5.2 Descriptive Statistics

The statistical tools like mean, S.D. and C.V. have been used in the study.

Arithmetic Mean or Average ($\overline{X}$)

An average represents a group of values. It depicts the characteristic of the whole group. It is an envoy of the entire mass of homogeneous data. Generally, the average value lies

somewhere in between the two extremes i.e. the largest and the smallest items. It is calculated as follows:

$$Aithmetic\ Mean\ (\bar{X}) = \frac{x_1 + x_2 + x_3 + \ \ldots\ldots\ldots + x_n}{N}$$

$$\bar{X} = \frac{\sum X}{N}$$

Where,

$\sum X$ = Sum of the sizes of the items N = Number of items

Standard Deviation (σ)

Karl Pearson first introduced the concept of standard deviation in 1983. Standard deviation is the positive square root of the arithmetic average of the squares of all the deviation measured from the arithmetic average of the series. The standard deviation measures the absolute dispersion of a distribution. Greater the amount of dispersion the greater the standard derivation i.e. greater will be the magnitude of the deviation of the values from their mean. A small standard deviation means a high degree of uniformity of the observation as well as homogeneity of a series. Standard Deviation is denoted by a Greek letter 'σ' (Sigma) and is calculated as follows.

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

Where,

N = Number of items in the series.

$\bar{X}$ = Mean X = Variable

Coefficient of Variation (C. V.)

It is the measurement of the relative dispersion by Karl Person. It is used to compare the variability of two or more series. The series with higher coefficient of variation is said to be more variable, less consistent, less uniform, less stable and less homogenous. On the contrary the series with less coefficient of variation is said to be less variable, more consistent, more uniform, more stable and more homogenous. It is denoted by C.V. and is obtained by dividing the standard deviation by arithmetic mean. Thus,

$$\text{Coefficient of Variation (C.V.)} = \frac{\sigma \text{ X } 100}{\overline{X}}$$

Where,

σ = Standard Deviation $\overline{X}$= Mean

3.5.3 Correlation Coefficient (r)

The correlation analysis is a technique used to measure the closeness of the relationship between the variables. It helps us in determining the degree of relationship between two or more variables. It describes not only the magnitude of correlation but also its direction. The coefficient of correlation is a number which indicates to what extent two variables are related with each other. Similarly, what extent variations in one lead to the variation in the other?

The value of coefficient of correlation always lies between ± 1. A value of -1 indicates a perfect negative relationship between the variables and a value of +1 indicates a perfect positive relationship. A value of zero indicates that there is no relation between the variables. The zero correlation coefficient means that the variables are uncorrelated. The closer r is +1 or -1, the closer the relationship between the variables and closer r is to zero (0), the less close relationship. The algebraic sign of the correlation coefficient indicates the direction of the relationship between two variables. It may be direct or inverse.

Thus, in this study, the degree of relationship between the market price and other relevant financial indicators such as dividend per share, earning per share, and dividend payout ratio are measured by the correlation coefficient. The correlation coefficient can be calculated as;

$$r = \frac{Cov(XY)}{\sigma_x \sigma_y}$$

$$r = \frac{\Sigma(X - \bar{X})(Y - \bar{Y})}{(N-1)\sigma_x \sigma_y}$$

Or,

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

Where,

σ_x ,σ_y are the standard deviation of the distributions of X and Y values respectively.

Cov (X, Y) = Co variation of X, Y value

$$= \frac{\Sigma(X - \bar{X})(Y - \bar{Y})}{N}$$

Under this study, the correlation between the following variables is analyzed:

a) Dividend per Share and Earning Per Share.

b) Dividend per Share and Net profit.

c) Dividend per Share and Market price per share.

d) Dividend per Share and Net Worth.

e) Multiple Correlation among dependent and independent variable have been calculated.

3.6 Data and Variables

The empirical investigation conducted for a large sample of the companies listed in the Nepal stock Exchange market during the period 2004/05-2008/09. For a firm to be included in the sample, the firm had to list in the stock exchange market for the whole of the period under consideration. This condition was imposed to ensure that dividend policy was not distorted by the effects of a recent official listing.

In order to examine empirically the dividend model, the key variables of interest are the: measures of dividend (D), distributed earnings (DE). Net interest (S) and changes in this year's distributed earnings and dividend from this year to the year before (ΔDE and ΔD). These variables were derived from data collected from the database of the Nepal stock exchange. Dividend ($D_{i,t}$) as the distributed earnings of the firm i at time t, size ($S_{i,t}$) as the total interest earning of the bank, change in the distributes earnings ($\Delta DE_{i,t}$) as $DE_{i,t}$ - $DE_{i,\,t-1}$ and in last year's dividends (ΔD) as $D_i - D_{t-1}$.

3.7. The Model

In order to proceed the analysis of the data methods designed for panel data were used. The use of panel data models is a powerful research instrument, since it combines the cross-section data with time- series data and provides result that could not be estimated and studied if only time –series or cross-section data with time-used. A general model for panel data that allows this study to estimate panel data with great flexibility and formulate the differences.

This study tests the explanatory power of a model based on the distributed earning of the firm and its size having a long run target payout ratio, not only by the known changes in dividend parameter but also by the changes in distributed earnings, the econometric presentation of the model is:

$$D_{it} = a_i + \beta_1 DE_{it} + \beta_2 S_{it} + \beta_3 \Delta D_{i,t} + \beta_4 \Delta DE_{it} + \varepsilon_{it}$$

Where D_{it} = the dividend of the firm I at time t, DE_{it} = the distributed earnings of the firm i at time t, $\Delta D_{it} = D_{it} - DE_{i,t-1}$ the change between the distributed earnings at time t and time t-1, for the firm i and ε_{it} = the error at t.

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CAPTER IV

PRESENTATION AND ANALYSIS OF DATA

Dividend policy is a major decision of the firm due to its decision of dividing net earnings into two parts: the retained earnings and dividends and its impact upon value of the firm. The study contains different objectives, which have already mentioned in the previous chapter. In order to fulfill these objectives, the study attempts to analyze the secondary data regarding dividend policy of joint venture Banks (JVSs). The analysis includes several tools and techniques such as statistical and financial indicators as well as the attitude of management towards the optimum decision. This analysis is highly supported by the practice of dividend distribution by JVBs. Presentation and interpretation of financial statement is done here to determine the meaning of financial data.

4.1 Analysis of the Financial tools (indicators)

4.1.1 Earning Per Share (EPS)

Normally, the performance and achievement of a business organization are measured in terms of their capacity for generating earnings. Higher earning indicates the strength and lower earning denotes the weakness of business organization. Earning per share is calculated by dividing the net profit after taxes (NPAT) by the total number of common shares outstanding. EPS is the measurement of good and bad performance of institutions. For instance, higher EPS shows the good performance and lower EPS shows the weak performance. As a result, EPS, the achievement of the institutions are measured with the help of its capacity to generate higher earning per share. So, higher EPS is the important financial tools (factors) of business organization to achieve its goals and objectives. The earning per share of the bank under study is tabulated as follows:

Table 1
Analysis of Earning Per Share (EPS)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	105.49	129.21	137.08	108.31	106.76	117.37	14.70	12.53
NIBL	39.5	59.5	62.6	57.9	37.4	51.4	11.9	23.2
HBL	47.91	59.24	60.66	62.74	61.90	58.49	6.06	10.36
SCBNL	143.14	175.84	167.37	131.92	109.99	145.65	26.69	18.33
EBL	54.22	62.78	78.42	91.82	99.99	77.45	19.17	24.76

Source: www.sebon.org.np

The EPS of NABIL Bank Ltd. ranges between Rs.137.5 and Rs.105.49 during the period of the study. In this period the average EPS or mean is Rs.117.37. It means NABIL has made Rs.117.37 as the annual average EPS. The Standard Deviation of the EPS under the period of the study is 14.70 which indicates the other data of EPS are averagely varied from the mean by 14.70. The Co-efficient of variation (C.V.) of this bank is 14.46% on EPS. It indicates that there is 12.53% fluctuation in EPS during five years.

Nepal Investment Bank Ltd. (HIBL) has an average EPS of Rs.51.4 with a standard deviation of 11.9. The EPS ranges within 62.6 to 37.4. The Coefficient of variation is 23.2%, which shows that there is highly fluctuated in EPS of that Bank.

The average EPS of Himalayan Bank Ltd (HBL), during this period of study, is Rs.58.49 It stays within the range of Rs.62.74 to 47.91. The standard deviation of EPS is 6.06 where as the co-efficient of variation 10.36. The CV indicates a moderate fluctuation in the EPS of the Bank.

Likewise, Standard Chartered Bank Nepal Ltd. is successful to have average EPS of Rs.145.65 within the range from167.37 to 109.99. The other EPS amounts are varied from the mean (145.65) by the standard deviation of 26.69. the average fluctuation in EPS within the 5 years by 18.33%.

Similarly, Everest Bank Ltd. (EBL) has the average EPS of Rs.77.45 within the ranges from 99.99 to 54.22. alon with the standard deviation of 19.17. The average annual fluctuation is 24.76% in EPS of this bank.

Table-1 shows EPS of sampled commercial banks in Nepal seems to be positive. The average EPS of SCBNL is the highest and that of HBL is the lowest. The EPS range of the banks under study during this period is between Rs.167.37 to Rs.37.4. Similarly, the standard deviation of SCBNL is the highest and HBL is the lowest. The coefficient of variation of these banks shows that there is fluctuation in the EPS. If we compare the entire banks, HBL has the most consistent EPS among all the sample banks.

4.1.2 Dividend Per Share (DPS)

Dividend per share indicates the proportion of earning distributed to owner (shareholder) on per share basis. Generally, the higher DPS creates positive attitude among the shareholders toward the bank, which accordingly helps to increase the market value of shares. The dividends per share of the banks under study are stated in the table below.

Table 2
Analysis of Dividend Per Share (DPS)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	70	85	100	60	35	70	24.75	35.36
NIBL	12.5	20	5	7.5	20	13	6.94	53.36
HBL	11.58	60	15	25	12	24.72	20.46	82.76
SCBNL	120	130	80	80	50	92	32.71	35.56
EBL	0	25	10	20	30	17	12.04	70.83

Source: www.sebon.org.np

Table 2 shows the average DPS of NABIL Bank Ltd. is Rs.70. It is within the range of Rs.100and Rs.35. The standard deviation of DPS is 24.75 whereas the coefficient of variation of 35.36% indicates there is quite fluctuation in DPS of NABIL Bank Ltd.

The average DPS of Nepal Invested Bank ltd. (NIBL) is Rs.13 within the range of Rs.20 and Rs.5 where as the standard deviation appeared as 6.94 with the coefficient of variance of 53.36 which shows the high fluctuation in DPS of NIBL in period of 5 years.

Himalayan bank ltd. (HBL) has low average DPS of Rs.24.72 remaining in the range of RS.60 to Rs.11.58. The other DPS of this bank are varied of 20.46 as seemed as standard deviation. The coefficient of variance explains that this bank has faced very high fluctuation of 82.76 in 5 years. It has less steady in DPS trend.

Mean DPS of Standard Chartered Bank Nepal Ltd. (SCBNL) is Rs.92 with the standard deviation of 32.71. The highest and lowest DPS are Rs.130 and 50 respectively. The coefficient of variation is 35.56%, this indicates that there is moderate fluctuation in the DPS of SCBNL during the period of the study.

Everest Bank Ltd. has an average DPS of Rs17. The highest DPS is Rs.30 whereas it has not paid dividend in the year 2004/05.The standard deviation is 12.04 and coefficient of variation is 70.83%. The CV indicates that the DPS of NSBL is highly fluctuating.

From the findings, SCBNL has the highest average DPS and NIBL has the lowest. The C. V. indicates that among the banks under study during period, NABIL has the highest consistency in paying dividend whereas the DPS of HBL is highly fluctuating.

4.1.3 Dividend Payout Ratio (DPR)

This Ratio shows the amount of dividend as a percentage of earning available for equity share. It depends upon earnings of organization. Greater the earning is the more ability to pay dividend. The DPR of the banks under study are stated in the table as follows.

Table 3
Analysis of Dividend Payout Ratio (DPS)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	66.36	65.78	72.95	55.40	32.78	58.65	15.77	26.88
NIBL	31.65	33.61	7.99	12.96	53.45	27.93	18.16	65.01
HBL	24.17	101.28	24.73	39.85	19.39	41.88	34.08	81.38
SCBNL	83.83	73.93	47.80	60.64	45.46	62.33	16.55	26.55
EBL	0.00	39.82	12.75	21.78	30.00	20.87	15.37	73.64

Source: www.sebon.org.np

NABIL Bank Ltd. has an average DPR of 58.65% during this period of study. It means that it generally pays average 58.56% of its earning to its shareholders in form of dividend in every year. The standard deviation of DPR was 15.77 whereas the coefficient of variation of 26.88% indicates the less fluctuating nature of DPR in NABIL Bank Ltd.

The average DPR of Nepal Investment Bank Ltd. is 27.93 which describes this bank has been allocated 27.93% of its net income as the annual average dividend to its

shareholders. The other DPR data are varied from mean DPS (27.93%) by an average of 18.16(St.Dev). The coefficient (65.01) of DPR of this bank shows the high fluctuation in DPR in the study period.

Likewise, Himalayan Bank Ltd. had distributed 41.88% of the total earning as annual average dividend payout ratio. Its standard deviation is 34.08 with the coefficient of variance 81.38 which indicates the high fluctuation in DPR of this bank.

The average DPR of Standard Chartered Bank Nepal Ltd. (SCBNL) is 62.33%. It means that SCBNL generally pays 62.33% of its total earning as dividend to its shareholders. The standard deviation of DPR is 16.65. The coefficient of variation is 26.55%, which indicates that there is only about 26.55% fluctuation in DPR of the bank over the years.

An average DPR of 27.14% of Nepal SBI Bank Ltd. (NSBL) indicates that NSBL generally pays out 27.14% of its earning as dividend. The standard deviation is 29.02 and coefficient of variation is 106.9%. The C. V. indicates that the DPR of NSBL is highly fluctuated during the period of study.

Similarly, Everest Bank Ltd. has average DPR of 20.87%, it means around 20.87% of the total earning has been distributed to the shareholders as the annual average dividend. The standard deviation (15.37) describes that DPR of the 5 years are varied from the mean by 15.37.

The above calculation shows that SCBNL has the highest mean DPR and it also has the lower CV on DPR. It shows that SCBNL has the uniform dividend payments trend. On the other hand the CV of hBL is high which indicates high oscillation in their DPR.

If analysis is done taking the mean DPR of the sample banks, the average dividend payout ratio of the sample banks comes out to 55.5 with a standard deviation of 15.02 and CV of 43.22%. It indicates that, in average, out of the total earnings made 55.5%% is distributed as dividend to the shareholders with fluctuation of 43.22%.

4.1.4 Market Price Per Share (MPS)

MPPS is the price of share on which shares are traded in the secondary market. Thus, this price is fixed in the stock market on the basis of demand and supply position for a specified share. Higher MPPS is more desirable. The average market price per share of the banks under study is presented in table as follows.

Table 4
Analysis of Market Price Per Share (MPS)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	1505.00	2240.00	5050.00	5275.00	4899.00	3793.80	1778.09	46.87
NIBL	800.00	1260.00	1729.00	2450.00	1388.00	1525.40	614.79	40.30
HBL	920.00	1100.00	1740.00	1980.00	1760.00	1500.00	461.52	30.77
SCBNL	2343.00	3775.00	5900.00	6830.00	6010.00	4971.60	1853.05	37.27
EBL	870.00	1379.00	2430.00	3132.00	2455.00	2053.20	911.28	44.38

Source: www.sebon.org.np

The average of closing MPS of NABIL Bank Ltd., during the study, is Rs.3793.80. It stays within the range of Rs.5275 and Rs.1505. The standard deviation of closing MPS is 1778.09 whereas the coefficient of variation is 46.87%. The CV indicates moderate fluctuation in the closing MPPS of the bank.

Nepal Investment Bank Ltd. has average closing MPS of Rs.1525.40 with the range of Rs.2450 and Rs.800. Its standard deviation is 614.79 with the C.V. of 40.30%. its indicates that there is fluctuation if 40.30% in the MPS of this bank under the study period.

Rs.1500 is the average MPPS of Himalayan Bank Ltd. staying in the range of RS.1980 and Rs.920 with the standard deviation of 461.52. The C.V. of 30.77% shows the lower fluctuation trend in MPPS of this bank.

The average of closing MPS of Standard Chartered Bank Nepal Ltd. during the period of study is Rs.4971.6 with a standard deviation of 1853.05 and a coefficient of variation of 37.27%.

Similarly, Everest Bank Ltd. (HBL) has an average closing MPS of Rs.2053.20 with a standard deviation of 911.28. The coefficient of variation shows that there is a fluctuation of 44.38% in closing MPPS of NSBL.

Finally, the average MPPS of SCBNL is higher than other banks. So this bank is in good position but the average MPPS of all sample commercial banks are considered to be encouraging. Almost all banks' MPPS is in increasing trend up to financial year 2007/09 then in decreasing trend. There is less fluctuation in the MPPS of SCBNL and HBL they have lower coefficient of variation. The MPPS of sample banks have fluctuated in range of 30.77% to 46.87% as indicated by respective C.V of the different sample banks.

4.1.5 Price Earning Ratio (P/E Ratio)

Price-earning ratio is the between market price per share and the earning per share. It is also known as earning multiplier. The price- earning ratio of the banks is presented in table below.

Table 5
Analysis of Price Earning Ratio (P/E Ratio)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	14.27	17.34	36.84	48.70	45.89	32.61	15.99	49.04
NIBL	20.25	21.23	27.63	42.33	37.10	29.71	9.74	32.79
HBL	19.20	18.57	28.69	31.59	28.43	25.30	5.99	23.67
SCBNL	16.38	21.47	35.25	51.77	54.64	35.90	17.27	48.10
EBL	16.04	21.97	30.99	34.11	24.55	25.53	7.20	28.18

Source: www.sebon.org.np

The table shows, NABIL Bank Ltd has an average P/E ratio of 32.61. The standard deviation is 15.99 and coefficient of variation is 49.04%. The CV indicates that P/E ratio of NABIL Bank Ltd is quite fluctuating.

The average P/E Ratio of NIBL, during the study, is 29.71. It is within the range of 42.33 and 20.25. The standard deviation of P/E Ratio is 9.47 whereas the coefficient of variation of 32.079% indicates the fluctuating nature of P/E Ratio in MIBL.

HBL has an average P/E ratio of 25.30, ranging between 31.59 and 18.57 during the period of study. The standard deviation of 5.99 and the fluctuation of 23.67% in the P/E ratio are seen during this period which is low.

Likewise, the average P/E Ratio of SCBNL, during this period of study, is 35.90. It is within the range of 54.64 and 16.38. The standard deviation of P/E Ratio is 17.27 whereas the coefficient of variation of 48.10% indicates the fluctuating nature of P/E Ratio in SCBNL.

From the calculation, SCBNL has the highest average P/E Ratio and HBL has the lowest. The C.V indicates that among the banks under study during the period HBL has the highest consistency in P/E ratio whereas the P/E ratio of NABIL is highly fluctuating.

4.1.6 Earning Yield (EY)

Earning yield is the percentage of earning per share to market price per share in the secondary market. It gives an idea of how much an investor might get for his money. The share with higher earnings yield is worth buying. Earning yield of the banks under the study is presented in the table below.

Table 6
Analysis of Earning Yield (EY)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	7.01	5.77	2.71	2.05	2.18	3.94	2.29	57.98
NIBL	4.94	4.72	3.62	2.36	2.70	3.67	1.16	31.61
HBL	5.21	5.39	3.49	3.17	3.52	4.15	1.05	25.39
SCBNL	6.11	4.66	2.84	1.93	1.83	3.47	1.86	53.55
EBL	6.23	4.55	3.23	2.93	4.07	4.20	1.31	31.08

Source: www.sebon.org.np

The average EY of NABIL Bank Ltd, during this period of study, is 3.94%. It is within the range of 7.01% and 2.05%. The standard deviation of EY is 2.29 whereas the coefficient of variation is 57.98%. The coefficient of variation in EY of NABIL indicates that it has above moderate fluctuation.

The average EY of Nepal NIBL is 3.67%. The standard deviation is 1.16% and coefficient of variation is 31.61%. The C.V indicates that the EY of NSBL is moderate fluctuating.

HBL has the average DY of 4.15% with the standard deviation of 1.05 where as the coefficient of variance (25.29%) shows the low trend of fluctuation in DY on this bank in 5 years.

The average of EY of 3.47 with the standard deviation of 1.86 is seen for SCBNL. The highest and the lowest EY are 6.11% and 1.83% respectively. The coefficient of variation is 53.55% during the period of study.

The average EY of Nepal EBL is 4.20%. The standard deviation is 1.31% and coefficient of variation is 31.08%. The C.V indicates that the EY of EBL is less fluctuating.

The findings indicate, EBL has the highest average EY and SCBNL has the lowest. The C.V indicates that among the banks, during the period of study, HBL has the highest consistency in its earning yield whereas the earning yield of NABIL is highly fluctuating.

4.1.7 Dividend Yield (DY)

Dividend yield is the percentage of DPS on MPPS. It measures the dividend in relation to market value of share. It is the dividend received by the investors as a percentage of market prices per share in the stock market. This ratio highly influences the market price per share because a small change in dividend per share can bring effective change in the market value of the share. The dividend yields of the banks, under the period of the study are presented in the table given below.

Table 7
Analysis of Dividend Yield (DY)

Banks	2004/05	2005/06	2006/07	2007/08	2008/09	Avg.	St. Dev	C.V.
NABIL	4.65	3.79	1.98	1.14	0.71	2.46	1.70	69.38
NIBL	1.56	1.59	0.29	0.31	1.44	1.04	0.68	65.31
HBL	1.26	5.45	0.86	1.26	0.68	1.90	2.00	105.09
SCBNL	5.12	3.44	1.36	1.17	0.83	2.38	1.84	77.19
EBL	0.00	1.81	0.41	0.64	1.22	0.82	0.71	86.97

Source: www.sebon.org.np

The table-7 describes, the average DY of NABIL Bank Ltd during this period of study is 2.46%. It stays within the range of 4.65% and 0.71%. The Standard deviation of DY is 1.70 whereas the coefficient of variation is 69.38%. The C.V indicates a high fluctuation in the DY of the bank.

Nepal Investment bank Ltd. has an average DY of 1.04% with a standard deviation of 2. The DY ranges between 1.59% and .0310%. The coefficient of variation shows that there is a fluctuation of 65.31% in DY of NIBL.

Likewise, the average DY of Himalayan Bank Ltd. is 1.9% staying in the rage of 5.45% and 0.68% with the standard deviation of 2. The coefficient of 105.09% shows the very high fluctuation in dividend yield of this bank in 5 years.

The DY of Standard Chartered Bank Nepal Ltd. ranges between 5.12% and 0.83% during the period of study. During this period, the average DY is 2.38%. The standard deviation DY of SCBNL under the period of study is 1.84. The C.V. of 77.19% indicates that the fluctuation of DY of SCBNL is the high.

Finally, EBL has the average DY is .082 within the range from 1.22% to 0%. The standard deviation is 0.71 along with C.V. of 86.97%.It indicates there is high fluctuation in dividend yield in this bank in the observed five years.

In conclusioin, it can be explained that the average DY of HBL is the highest and that of EBL is the lowest. The DY range of the banks, during the period of study is between 5.12% and 0%. Similarly, the standard deviation of HBL is the highest and NIBL is the lowest. The coefficient of variation of these banks shows a high level of fluctuation in the DY. All the sampled banks have high fluctuation in dividend yield indicator.

4.2 Analysis of Descriptive Statistics

Statistical tools have been used to provide meaningful relationship among the various interrelated variables. In statistical analysis, degrees of correlation between dividends with other variables have been established. Simple regression analysis has been used to know how one variable is related with other variables and the impact of dividend policy followed by the sampled banks. Similarly, mean, standard deviation, percentile, covariance and coefficient of determinants. The following table shows the Mean, Median, Standard Deviation and Percentile.

Table 8
Result of Descriptive Analysis

	Total Dividends(Rs)	Distributed Earning(RS)	Interest Income(Rs)	Differential Dividend	Differential Earnings
Mean	421860635.00	542297462.36	1592834819.68	80557202.92	66348030.96
Median	417906240.00	536260260.00	1584987354.00	67052700.00	115959343.00
Std. Deviation	236939048.88	234994454.42	660250658.59	96919047.25	180029249.56
Percentiles 25	243052890.00	329406820.50	1158575250.50	0.00	16448439.50
50	417906240.00	536260268.00	1584987354.00	67052700.00	115959343.00
75	53350377.50	693884221.00	1971172099.50	131712787.50	150021980.00

Source: www.sebon.org.np

Table-5 shows that the average dividend distribution of sampled banks is RS.421860635 during the study period from 2004/2005 to 2008/2009. This result indicates that the sampled commercial banks distribute average annual dividend of Rs.421860635. the standard deviation is 236939048.88 which interprets that the remaining all observed dividend amount are varied with the mean dividend amount by 236939048.88. Among

the sampled banks, it is seemed that around 25 percent of the sampled banks' total dividend is distributed below Rs.243052890, 50 percent (median) is Rs. 417906240. Similarly, more than 75% of the dividend distribution is over Rs. 533507377.

In the regard of distributed earning, the annual average distributed earning is Rs. 542297462.36 with the standard deviation of 234994454.42. It means that there is average variation of data of distributed earnings with the mean. The percentile explain that the 25% of the total data of the this variables shows the distributed earning of Rs. 329406820.50, median (50%) is Rs.536260268.00 and the distributed earning of Rs. 693884221.00 lies above the 75% of the data.

Incase of interest income, the annual average income of sampled commercial banks is Rs1592834819.68 along with standard deviation of 660250658.59. The standard deviation means the entire data of interest income are varied from the mean value (Rs1592834819.68) by 660250658.59. And percentiles analysis the data in total of 100% where 25% of the overall data of interest income is below Rs. 1158575250.50, the mid value (median) is Rs.1584987354.00 and more than 75% of the data is above Rs. 1971172099.50.

There is an annual average of Rs.80557202.92 of differential earnings with standard deviation of 96919047.25. This result indicates that rest data of this variable of sampled commercial banks is varied from the mean value by 96919047.25. The mid value of this data is131712787.50 and more than 75% of the entire data is over Rs. 131712787.50.

Finally, there is an annual average differential earning of Rs. 66348030.96. The standard deviation is 180029249.56 which indicate there is an average variation of 180029249.56. 25% of the total data of differential earning is below the Rs. 16448439.50 with the median (50%) of 115959343.00 and above 75% of the aggregate data is over Rs. 150021980.00.

4.3 Analysis of Correlation Coefficient

Correlation analysis helps us to determine how strongly the variables are correlated to each other. It is a statistical tool, which can describe the relationship or the degree to which one variable linearly related to another variable. The analysis is a useful statistical tool, which describes the relationship of the variables in following ways; whether the relationship is positive or negative, whether the relationship between the variables exists or not. Here the correlation analysis is referred to identify the relationship between dependent and independent variables.

Table 9
Result of Correlation Coefficient Analysis (N=25)

	Total Dividends(Rs)	Distributed Earning(RS)	Interest Income(Rs)	Differential Dividend	Differential Earnings
Total Dividends(Rs) Pearson correlation	1.000	0.574**	0.516**	0.471*	-0.249
Sig.(2-tailed)		0.003	0.008	0.018	0.231
Distributed earning(Rs) Pearson Correlation	0.574**	1.000	0.641**	0.238	0.597**
Sig.(2-tailed)	0.003		0.001	0.252	0.002
Interest Income(Rs) Pearson Correlation	0.516**	0.641**	1.000	0.205	
Sig.(2-tailed)	0.008	0.001		0.325	0.227
Differential Dividend Pearson Correlation	0.471*	0.238	0.205	1.000	0.276
Sig.(2-tailed)	0.018	0.252	0.325		
Differential Earning Pearson Correlation	-0.249	0.597**	0.227	0.060	1.000
Sig.(2-tailed)	0.231	0.002	0.276	0.774	

** Correlation is significant at the 0.01 level (two tailed)

*Correlation is significant at the 0.05 level (two tailed**)**

Table-6 indicates that independent factor (total dividend) is correlated with the variable factors at different significant level. The correlation coefficient between total dividend and distributed earning is 0.574(0.003). The correlation between these two variable is statistically significant at 1% level (2-taied). It indicates that these two variables have highly positive correlation.

Likewise the correlation between total dividend and interest income is 0.516(0.008).this result describe that there is statistical significant between these two variables at 1% level (2-taied). It shows that these two variables have high positive correlation.

The total dividend is also correlated with differential dividend as there is correlation between them is 0.471(0.018). So there is also statistic significant at 5% level (2-tailed). Both have low positive correlation.

Not only dependent and independent variables are correlated but also there is correlation between independent variables. The correlation coefficient between two independentt variables distributed earnings and interest income is 0.641(.001). The correlation coefficient between there two variables is statistically significant at 1% level (2-tailed). So they have high positive correlation.

The pair of independent variables distributed earnings and differential earning also have correlation coefficient of 0.597(0.002). They have statistic significant at 1% level (2-tailed).it indicates that these two variables have high positive correlation.

4.4 Analysis of Regression Result

When we know the value of one variable and we have to estimate the value of another variable, we need regression analysis to calculate the values of an unknown variable. In other words, it is a statistical tool, which helps us to estimate the value of one variable when another variable is known. Regression analysis is a general process of predicting one variable from another by using statistical means. Regression is the estimation of unknown values or prediction of one variable from known values of other variables. The estimation of regression plays a vital role in every step of many sectors.

Table 10
Result of Regression Analysis
$(D_{it} = a_i + \beta_1 DE_{it} + \beta_2 S_{it} + \beta_3 \Delta D_{i,t} + \beta_4 \Delta DE_{it} + \varepsilon_{it})$

Explanatory	coefficients	t-Stat	Prob. (t-Stat)
Constant	-1.2E+07	-3.251	0.004
DE	1.05	11.875	0
S	-0.003	-0.11	0.914
ΔD	0.68	5.077	0
ΔDE	-1.165	-12947	0
R^2	0.944		
Adj. R^2	0.933		
Durbin-Watson	1.522		

The table-10 indicates that the adjusted R^2 is 0.933. This result indicates that the 93.3% of the amount of dividend paid by the firm can be explained by the variables tested. It is obvious that he constant term is statistically significant. All that the independent variables proved to be very useful and very high t-statistic except interest income, which indicate that are significant in level of confidence 99 percent. The distributed earning of the firm is positively related with the dividend of the firm. The greater amount from earnings that are going to be distributed the greater the dividend accordingly.

The result shown in table-10 indicates that distributed earnings (DE), Differential Dividend (ΔD) and Distributed earning(DE) are the independent variables that affects the payment of annual dividend in sampled commercial banks of Nepal.

4.5 Major Findings

The major findings of this study work are summarized in numeric order given below:

1) The average earning per share (EPS) of the banks under the study shows a positive result. But the coefficient of variation indicates that there is less consistency of EPS. The C.V ranges within 24.76% to 10.36%. Among the sample banks SCBNL has the highest average EPS with the less fluctuation and HBL has the least with high degree of fluctuation.

2) The average dividend per share (DPS) shows that there is no regularity in dividend payment. The SCBNL has the highest average DPS and the higher degree of paying regular dividend to their shareholders. DPS share also fluctuating. The C.V. of DPS ranges within 82.76% to 35.36%. NIBL has the lowest average DPS and HBL has highest fluctuation among the sample banks.

3) The analysis of DPR also shows that the DPR of the banks are not stable. Among the banks under the study, SCBNL has the highest average DPR and NABIL has least fluctuation in the DPR. The result also shows that NIBL has the lowest average DPR and has the high fluctuation. The fluctuating ranges within 81.38% to 26.55%.

4) The average market price per share (MPS) shows that there is quite high level of fluctuation. SCBNL has higher average MPS than other banks. So, this bank is in good position but average MPPS of all commercial banks being considered to be encouraging. HBL has the lowest average MPS but lowest fluctuation and NABIL has the highest fluctuation.

5) The average price-earning ratio (P/E) of SCBNL among the banks under the study is the highest and also highly unstable. The ratio of remaining banks and financial companies are satisfactory and slightly stable.

6) The average earning yield of banks, under the study, indicates that the earning yield of EBL is higher than other banks. The mean EY of different banks ranges from 4.20% to 3.47%. The EY of HBL is less fluctuated than other banks. But NABIL has higher fluctuation in its earning as indicated by C.V. of this bank.

7) The average dividend yield of the banks indicates that the dividend yield is quite low ranging within 2.46% to 0.82%. Among the banks, NABIL has the highest average dividend yield and EBL has the lowest. There is high fluctuation in the dividend yield ranging from 105.09% to 65.31%.

8) The average annual dividend distribution of sampled commercial banks is Rs.421860635.00.

9) The total dividend is highly positively correlated with the factors distributed earnings and interest income whereas distributed earnings and interest income have also high positive correlation of coefficient. But the total dividend has low positive correlation with differential dividend.

10) The independent variables like distributed earning, differential dividend, and distributed earning affect the payment of annual dividend in the sampled commercial banks in Nepal.

CHAPTER-V
SUMMARY, CONCLUSION AND RECOMMENDATIONS

A brief description regarding dividend policy and practice of commercial banks has been already presented in the previous chapters. A brief introduction of the study has been presented in the first chapter. Besides, the review of literature with possible review of ideas, theories and research findings has also been presented in the second chapter. Research methodology has been described in the third chapter where all the available data are presented and analyzed in the fourth chapter as well as findings are also drawn related to dividend policy in these sample commercial banks.

Therefore, in this chapter, summary and conclusion regarding the study topic are presented. These findings regarding dividend policy certainly have shown necessity for the improvement of existing condition of the commercial banks of Nepal. So, the analysis of dividend, carried out from many dimension has provided some substantial feedback for the further improvement of the performance of the financial institution.

5.1 Summary

Dividend policy decision is one of the major decisions of financial management. The dividend policy decision affects on the operation and prosperity of the organization because it has the power to influence other two decisions of the organization i.e. capital structure decision and investment decision. An investor expects two types of return namely capital gain and dividend by investing in equity capital or ordinary share. So, payment of dividend to shareholders is an effective way to attract new investors and maintain present investors. It is important to have clearly defined and effectively managed dividend policy so as to fulfill the shareholders' expectations and corporate growth.

Dividend paying banks have been analyzed to show the implication of dividend policy that they have adopted in their market price per share. Now in Nepal, those banks have earned profit on only those paid dividend. Instability of dividend and inconsistent dividend payout ratio are the most applied phenomena of commercial banks in Nepal.

But, only the banks operating under Joint Venture are paying dividend more attractively than the banks promoted by indigenous promoters. However, dividend policy is taking its path, slowly in Nepalese Commercial Environment.

In analyzing the problem with the stated objectives, this study has been in more descriptive nature. The study covers three joint venture banks as well as it cover for the past five fiscal years from 2004/05 to 2008/098. The available secondary data has been analyzed using various financial and statistical tools. So, the reliability of conclusions of this study is determined on the accuracy of secondary data.

The theoretical statement of this study is that dividend decision should depend upon distributed earning and interest income of the sample banks. Among Sample Banks, dividend payout ratio of SCBNL is higher than other. Similarly, according to EPS, among sample banks, SCBNL is more successful than other where as NIBL is the lowest. On the basis of P/ E ratio, among sample banks, SCBNL has the higher ratio than other. It means SCBNL has the better performance for enhancing the wealth of shareholders rather than other banks. On the basis of DPS, SCBNL is paying higher value of dividend among sample banks. Moreover, on the basis of market price per share, SCBNL has higher MPS then others.

The regression model is used to interpret the relation between dependent variable(total dividend)and independent variables (distributed earnings, interest income, differential distributed earning and differential dividend), which results the independent variable distributed earning, differential dividend and differential earning affects the annual distribution of dividend to the shareholder in sampled commercial banks. .

The situation of capital market of Nepal is improving day by day. As a result, the capital market is efficient with compare to previous year. Though, there is **'weak'** efficient market where share price movement is random. This means share price movement does not follow any trends. In such market cash dividend will more effective then other forms of dividends like bonus and right. But it is reality that capital market of Nepal is still immature.

5.2 Conclusion

In conclusion, uncontrollable growth in number of financial institutions within a short span of time has raised reasonable doubts to the common people. By the analysis of investment activities, it is noticed that only few institutions have aggressive investment strategy with compare to conservative strategy among most of the financial institutions. Despite this, there is no doubt that financial institutions are the pillars of a nation's economy. The overall growth of the nation’s economy is linked with financial institutions. In these days, some financial institutions are running successfully and providing dividend to the shareholders according to their capacity. Also, they achieve the trust of common people which is the great success of their performance. On the whole, over this period, the scale of operation has expanded many times which makes more earnings every year. The financial institutions are able to distribute divided and able to expand their activities with the good earnings. But, it is yet to be done for the satisfaction of shareholders as well as overall growth of nation’s economy.

5.3 Recommendations

Based on the findings, the suggestions for future guidelines are presented here. These suggestions may also need some regressions but there is no doubt that these measures are helpful to improve the existing condition of financial institutions as well as other organizations of Nepal. These suggestions will be proved to be milestone in order to correct the existing situation.

a. Dividend policy is must for the enhancement of existing return to meet the expectation of shareholders as well as improvement of nation’s economy. By the formulation of dividend policy, there is a clear way to follow the dividend distribution. Therefore, the HMG must impose a minimum dividend obligation policy through suitable pragmatic legislative measure to ensure protection in the form of dividend payment to the investors in general.
b. Collective opinion should be taken from shareholders whether they prefer stock dividend or cash dividend. Issue of cash dividend increases MVPS and EPS. But issue of stock dividend decreases MVPS and EPS. Therefore, all the financial are suggested to decide about it after collective opinion from shareholders.

c. There is a lack of consciousness in Nepalese investors regarding their rights and the company act. Therefore, there should be a kind of educating center about their rights on dividend income and other specific rights. Every body should have clear knowledge about Nepalese Company Act- 1997 that makes some legal provisions for dividend payments.

d. Dividend equalization fund should be created from keeping aside some amount from profit to stabilize the payment of dividend to shareholders. At the time of lower earning dividend payout ration should be maintained from this fund.

e. Payment of dividend is neither static nor constantly growing. It is highly fluctuating. Such way of paying dividend could not impress the market positively. So, these financial institutions are advised to follow either static or constantly growing dividend payment policy. It would be better to fix the amount of dividend in the general annual meeting. This is important not only from the point of view of adequate return to shareholders but also to generate stable and increasing market value per share, long run survival of financial institutions, efficient management and socially acceptable distribution of income. Ability to maintain linkage of the adequate earning power with the adequate dividend return provides the benchmark for dynamic growth stability.

f. The fluctuation in EAT, EPS and DPR of the banks seems very high. The higher fluctuation shows that they are not going in targeted way. In this situation, banks are advised to fix their target rate of earring, payout ratio. That will help to build a good image in customers and shareholders and stock market.

g. Issue of stock dividend decreases market value per share and earning per share. But, issue of cash dividend increases market value per share and earning per share. So, due to this reason common shareholders should be given a choice whether they prefer stock dividend or cash dividend. Therefore, all the financial institutions are suggested to take care regarding the interest of shareholders.

h. As financial institutions are assisting to promote the capital market and improve the economic condition of nation through collecting the scattered resources and utilizing them into productive ways. The government should provide facilities to

improve the efficiency of the financial institutions and reduce the interference in daily affair. Similarly, the management should be careful about their duties and responsibilities for the operation of the financial institutions towards the interest of the shareholders as well as the improvement of nation's economy.

i. Formulation of dividend policy will clearly guide the way to follow dividend distribution. They should determine whether the company is going to adopt stable dividend policy, constant pay out ratio or low regular plus extra dividend. There should be the long run dividend payout ratio, either it is pure residual theory, fixed dividend payout policy or smoothed residual dividend policy they all should have been clearly explained by the dividend policy.

j. Since financial institutions are dealing with public money collected by way of deposits in different sectors, there should be active supervision and credit-monitoring role of NRB becomes important. Progress reporting should be continuous and financial institutions should make their performance transparent to the investors. Moreover, there should also be professional representation in the Credit Information Bureau instead of having only member of it.

k. All the financial institutions should conduct a seminar and workshop for shareholders to get experience at least twice in a year. Private consultancy firms' experts in financial activities and top executives from all the financial institutions should be the key participants in seminar to identify where the problems lie in the efficient operation. Only then, there will be the solution of the problems regarding the financial performance of the financial institutions, which are helpful for more profit as well as more dividends to their shareholders.

l. It is more important for financial institutions for long-term sustainability then getting quick rich tendency of short-term value. Since, financial institutions have to survive as institutions in the long run and provide capital gain to the investor. That's why all the financial institutions have to maintain certain discipline by learning from experience of operation regarding what is good to do and what is not good to do for future improvement and further success.

ANNEX

NABIL bank

Years	Total Divdend(Rs.)(D)	Distributd earning(DE)	Interest Income(S)
2004-2005	344158080	518646226	243544611
2005-2006	417906240	635266650	1309998500
2006-2007	688316160	673959851	1587758714
2007-2008	689216000	746489849	1978696727
2008-2009	820884950	1031031497	2798486196

EBL

Years	Total Divdend(Rs.)(D)	Distributd earning(DE)	Interest Income(S)
2004-2005	63000000	170793000	719297855
2005-2006	94500000	231030400	903411137
2006-2007	151200000	296427600	1144408308
2007-2008	245700000	480687480	1548657132
2008-2009	383292600	638757118	2186814992

NIBL

Years	Total Divdend(Rs.)(D)	Distributd earning(DE)	Interest Income(S)
2004-2005	73467312	232156707	886799959
2005-2006	327538996	350512791	1172742193
2006-2007	240405780	501406321	1584987354
2007-2008	491558657	696103884	2194275722
2008-2009	481413780	900725182	3267941142

HBL

Years	Total Divdend(Rs.)(D)	Distributd earning(DE)	Interest Income(S)
2004-2005	203217300	308300850	1446468083
2005-2006	270270000	457451280	1626473819
2006-2007	324324000	491837346	1775582617
2007-2008	456080625	635877742	1963647472
2008-2009	529783515	751837085	2342198176

SCBNL

Years	Total Divdend(Rs.)(D)	Distributd earning(DE)	Interest Income(S)
2004-2005	449568480	536260268	1058678000
2005-2006	524496560	658767679	1189603000
2006-2007	537231240	691664558	1411982000
2007-2008	807019200	818938252	1591195526
2008-2009	931966400	102506943	1887221257

Descriptive Statistics N=25

		Total Dividends (Rs)	Distributed Earning(Rs)	Interest Income (Rs)	Dffferential dividends	Differntial Earnings
N	Valid	25	25	25	25	25
	Missing	0	0	0	0	0
Mean		421860635.00	542297462.36	1592834819.68	80557202.92	66348030.96
Median		417906240.00	536260268.00	1584987354.00	67052700.00	115959343.00
Std. Deviation		236939048.879	234994454.420	660250658.591	96919047.249	180029249.564
Percentiles	25	243052890.00	329406820.50	1158575250.50	.00	16448439.50
	50	417906240.00	536260268.00	1584987354.00	67052700.00	115959343.00
	75	533507377.50	693884221.00	1971172099.50	131712787.50	150021980.00

Correlations

		Total Dividends (Rs)	Distributed Earning(Rs)	Interest Income(Rs)	Dffferential dividends	Differntial Earnings
Total Dividends(Rs)	Pearson Correlation	1	.574**	.516**	.471*	-.249
	Sig. (2-tailed)		.003	.008	.018	.231
	N	25	25	25	25	25
Distributed Earning(Rs)	Pearson Correlation	.574**	1	.641**	.238	.597**
	Sig. (2-tailed)	.003		.001	.252	.002
	N	25	25	25	25	25
Interest Income(Rs)	Pearson Correlation	.516**	.641**	1	.205	.227
	Sig. (2-tailed)	.008	.001		.325	.276
	N	25	25	25	25	25
Dffferential dividends	Pearson Correlation	.471*	.238	.205	1	.060
	Sig. (2-tailed)	.018	.252	.325		.774
	N	25	25	25	25	25
Differntial Earnings	Pearson Correlation	-.249	.597**	.227	.060	1
	Sig. (2-tailed)	.231	.002	.276	.774	
	N	25	25	25	25	25

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.972[a]	.944	.933	6.133E7

a. Predictors: (Constant), Differntial Earnings, Dfferential dividends, Interest Income(Rs), Distributed Earning(Rs)

ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.272E18	4	3.180E17	84.563	.000[a]
	Residual	7.522E16	20	3.761E15		
	Total	1.347E18	24			

a. Predictors: (Constant), Differntial Earnings, Dfferential dividends, Interest Income (Rs), Distributed Earning(Rs)

b. Dependent Variable: Total Dividends(Rs)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-120296479.051	37007296.650		-3.251	.004
	Distributed Earning(Rs)	1.050	.088	1.041	11.875	.000
	Interest Income(Rs)	-.003	.026	-.008	-.110	.914
	Dfferential dividends	.680	.134	.278	5.077	.000
	Differntial Earnings	-1.165	.090	-.885	-12.947	.000

a. Dependent Variable: Total Dividends(Rs)

Table 1
Regression Results

Variable	coefficients	t-Stat	Prob. (t-Stat)
Constant	-12029479.051	-3.251	.004
DE	1.050	11.875	.000
S	-0.003	-0.110	.914
ΔD	.680	5.077	.000
ΔDE	-1.165	-12947	.000
R^2 .944			
Adj. R^2 .933			
Durbin-Watson 1.522			

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.972[a]	.944	.933	6.133E7	1.522

a. Predictors: (Constant), Differntial Earnings, Diffferential dividends, Interest Income(Rs), Distributed Earning(Rs)

b. Dependent Variable: Total Dividends(Rs)

ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.272E18	4	3.180E17	84.563	.000[a]
	Residual	7.522E16	20	3.761E15		
	Total	1.347E18	24			

a. Predictors: (Constant), Differntial Earnings, Diffferential dividends, Interest Income (Rs), Distributed Earning(Rs)

b. Dependent Variable: Total Dividends(Rs)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-1.203E8	3.701E7		-3.251	.004		
	Distributed Earning(Rs)	1.050	.088	1.041	11.875	.000	.363	2.753
	Interest Income(Rs)	-.003	.026	-.008	-.110	.914	.550	1.820
	Diffferential dividends	.680	.134	.278	5.077	.000	.931	1.074
	Differntial Earnings	-1.165	.090	-.885	-12.947	.000	.597	1.674

a. Dependent Variable: Total Dividends(Rs)