

Is Cash Dividend an Everlasting Stimulus? Impact of Cash Dividend on Share Price of Manufacturing Companies in Sri Lanka

K. Charith^{1*} and A. Davydenko²

^{1*}*Department of Computer Science and Informatics, Uva Wellassa University, Badulla, Sri Lanka*

²*Independent Researcher, Antalya, Turkey*

Shareholder wealth consists of dividends and capital gain. The risk-return trade-off in these two returns drives the investor preference. The former is considered to be risk-averse whereas the latter is perceived to be risky. From one extreme dividend is a return for common stock to another a source of funding for public limited Companies. The objective of a for-profit organization is to maximize shareholder wealth, but disbursing dividends may not always in the best interest of shareholders. Theoretically retaining dividends may also increase share prices. The objective of the study was to measure the stimulus of cash dividends on share prices of 22 companies from 2011 to 2019, for 198 observations, listed on the Colombo Stock Exchange under the manufacturing sector. The novelty of this study is the use of advanced modeling and visualization techniques which eventually helped choose statistical methods with the most adequate assumptions. The Arellano Bond estimator is specifically selected given the nature of data properties and lagged variables. Market Price per Share (MPS) termed as the dependent variable whereas Dividend per Share (DPS), Dividend Payout Ratio (DPR), lagged MPS termed independent variables. The log of sales selected as a control variable through the forward selection criterion. The stationary tests performed, subject to log transformations and first differences revealed none of the variables are I (2). The results validated theoretical literature such as signaling effect and bird in hand theory but questioned previous empirical hypothesis. The study further validated cash dividends as a stimulus to investors given the strong positive relationship between DPS and MPS. The Granger Causality test reflected a short-term bidirectional relationship between MPS and DPS. This study sets a guideline for investors making the right investment choices and companies to keep the right balance between dividend policy and reinvestment strategies given the stimulus contained in dividends.

Keywords: Panel data, Dividends, Share price, Arellano bond estimator, Shareholder wealth