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INVESTORS ATTITUDE TOWARD DIVIDEND POLICY: A CASE STUDY ON KUWAITI BANKS

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Abstract

This study aims to identify investor's preference between cash dividend and capital gain. Despite the vast literature done on dividend policy, two theories stand above the rest, the first one is the bird in the hand theory and the other is the dividend irrelevance theory. Results of this research are based on a panel data of ten banks listed at Kuwait stock exchange over the period 2008-2018. Using ordinarily least square regression model, results showed that both dividend yield and dividend payout ratio had a statistically significant negative relation with banks share prices while earning per share had a statistically significant direct relation with share prices. These results supports dividend irrelevance theory which means that investors in Kuwaiti bank shares can be labeled as risk takers since they prefer uncertain capital gains over secured cash dividends.

Key words: Dividend policy, Kuwait stock exchange, Dividend irrelevance theory, Bird in the hand theory.

I. INTRODUCTION

The effect of dividend policy on share prices has always sparked debates among researchers. Some researchers such as Miller and Modigliani (1961) and Black and Scholes (1974) believe that dividends do not have any effect on share prices while others such as Gordon (1963) argues that dividends affects the share prices of companies. Black (1976) summarized that argument by stating that "*The harder we look at the dividend picture, it seems like a puzzle with pieces that don't fit together*". While many theories were developed to explain dividend theory such as agency theory, tax preference theory, transaction cost theory, signaling theory, and many others, only two theories stand above the rest which are dividend irrelevance theory and the bird in the hand theory. Dividend irrelevance theory (Miller and Modigliani, 1961) states that dividends have no effect on share prices and that reinvesting the net profit to perform better growth would lead to an increase in capital earnings for investors through increasing their share prices. In contrast, the bird in the hand theory (Gordon, 1963) believes that investors prefer dividends over capital gain

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since they are less risky and that companies should set a high payout ratio and offer high dividend yield to maximize their share prices.

Studies examining the effect of dividend policy on share prices produced conflicted results, while some studies supported Miller and Modigliani (1961) dividend irrelevance theory others supported Gordon (1963) bird in the hand theory. Studies supporting the dividend irrelevance theory would include the study by Jakata and Nyamugure (2014) when they used the data of selected firms on the Zimbabwean stock exchange (ZSE) over the period 2003-2011 and found no relation between dividend policy and share prices. AlAli et al. (2020) also examined the dividend policy effect on the share prices of insurance companies listed at Kuwait stock exchange over the period 2008-2018. They found that dividend yield and dividend payout ratio had a statistically significant negative effect on the share prices while earning per share had a statistically significant positive effect on share prices. Al Masum (2014) used the data of thirty commercial banks listed at Dhaka stock exchange over the period 2007-2011 and found that earning per share had a positive relation with share price while dividend yield had a negative effect on the share price. On the other hand, Ansar et al. (2015) used the data of 30 firms from textile, cement and chemical sector quoted at Karachi stock exchange in Pakistan over the period 2007-2011 and concluded that dividend had a positive relationship with share prices. Using the data of 163 companies listed at Nepal stock exchange for the fiscal year 2010-2011 to examine the relation between dividends and share prices, Joshi (2012) concluded that dividend had a significant effect on market prices. Ali et al. (2015) used the data of 45 non-financial companies listed on Karachi stock market in Pakistan over the period 2001-2012. They concluded that dividend payout ratio had a significant positive relationship with share prices which supports the bird in hand theory suggesting that shareholders give preference to assured cash dividends over uncertain cash of capital gains.

II. METHODOLOGY

This study attempts to examine the dividend policy effect on the share prices of commercial banks listed at Kuwait stock exchange over the period 2008-2018. A panel data is used to evaluate that relation where the share price is the dependent variable and dividend yield, earning per share, and dividend payout ratio as independent variables. The assumption is as follow;

$SP = f\,(DY, EPS, DPR)$

Which can be translated into the following equation;

$$SP = \alpha + \beta_1 DY + \beta_2 EPS + \beta_3 DPR + \varepsilon \qquad (1)$$

Where the variables are shown in table 1 as follow;

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Table 1. Variables Description

Variable	Symbol	Description
Share Price	SP	Market share price
Dividend Yield	DY	Dividend per share divided by share price
Earnings Per Share	EPS	Net profit divided by number of shares
Dividend payout ratio	DPR	Dividend per share divided by earning per share
Error Term	ε	

III. DATA AND EMPIRICAL RESULTS

This research is based on the data of ten commercial banks listed at Kuwait stock market over the period 2008-2018. The results of the research are based on their financial reports that were downloaded from Kuwait stock exchange and Kuwait institute of banking studies websites.

From table 2, it can be seen that the average share price of Kuwaiti banks during the study period was KWD 0.556 (1 KWD = USD 3.34) and the earning per share was KWD 0.025. Kuwaiti banks, on an average, paid dividend of % 34.3 of their profits while keeping the remaining % 65.7 to finance their future projects.

Table 2. Descriptive Analysis

Share Price	SP	DPR	DY	EPS
Mean	0.556	0.343	0.021	0.025
Standard Deviation	0.284	0.232	0.016	0.043
Kurtosis	0.374	-1.33	-1.264	32.985
Skewness	0.894	-0.61	-0.026	-3.113
Count	103	103	103	103

The ordinary least square regression (OLS) results, shown in table 3, reveals that the model was able to explain only 13.3% of the variation in share prices while the remaining 86.7% is explained by other variables. But despite that, the model can be labeled as a "good fit" since the significance *F* is less than 0.05. The results also shows that both dividend yield and dividend payout ratio had a statistically significant inverse relation with share prices while earning per share had a statistically significant direct relation with share prices. These results supports dividend irrelevance theory (Miller and Modigliani, 1961) while contradicting Gordon (1963) bird in the hand theory.

Table 3. OLS Regression output

R Square	0.158		
Adjusted R Square	0.133		
Significance *F*	0.0007		
Observations	103		
	Coefficient	**t Stat**	**P-Value**
Intercept	0.469***	10.017	0
DY	-11.327***	-3.066	0.003
EPS	1.759***	2.656	0.009
DPR	-0.812***	-3.281	0.001

*, ** , *** represent the confidence level at 90%, 95% and 99% respectively

IV. CONCLUSION

Using the data of Kuwaiti banks over the period 2008-2018, this research attempts to examine the effect of dividend policy on share prices. Results of the OLS regression model showed that both dividend yield and dividend payout ratio had a statistically significant inverse relation with share prices while earning per share had a statistically significant direct relation with share prices. These results supports dividend irrelevance theory (Miller and Modigliani, 1961) while it contradicts Gordon (1963) bird in the hand theory. Results obtained from this research also concludes that investors in Kuwaiti banks shares can be labeled as “risk takers” since they prefer uncertain capital gains over secured dividend payments.

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