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An effect of Dividend Policy on Nifty Company

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Abstract - The focus of this paper is on how dividend payments affect the value of a company. Creating a sustainable dividend policy is a difficult but crucial responsibility for every manager. Stock prices rise when dividends are distributed. The dividend is something the corporation strives for constantly. If the company wants to stay afloat, it needs to implement a consistent dividend policy that will keep investors happy and drive up the share price. The report analyzes data from 34 NIFTY 50 companies. You'll find businesses from the banking industry (eight firms), the auto industry (five firms), the energy sector (eight firms), the pharmaceutical industry (four firms), the IT industry (five firms), and the metal industry (five firms) (4 companies). The research spans the fifteen-year period from the 2004-05 to the 2018-19 academic years. Obtaining the necessary information from the Prowess database. Increased productivity, profitability, and share market value are just some of the benefits these industries will see as a direct result of the study's findings. A company's dividend policy sends a message to its investors about the company's health and growth, making it a crucial component of corporate finance. The dividend payout ratio and the amount of earnings retained by a company are directly related to the dividend choice made by the company, which is determined by the firm's dividend policy. Different factors, such as firm size, ownership, and other factors, influence the dividend decision. The study's goal is to examine the effects of dividend policy on the financial health and stock value of chosen companies. Secondary information was gathered from the prowess database.

Keywords - dividend, prowess database, company's dividend policy, profitability

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INTRODUCTION

A dividend is a distribution of a portion of a company's profits to its shareholders. A company's dividend policy is one of its most critical pillars. One of the primary functions of dividend policy is to communicate with existing shareholders and to entice potential new shareholders to the company. The choice to pay a dividend sets the proportion of profits distributed to shareholders and those kept by the company. The company's dividend policy is vital since it can have a significant impact on the value of its stock and its overall success. Dividend policy is an important part of corporate finance since it is used to send messages to shareholders about the company's health and future prospects. The firm's dividend policy will dictate how the company's profits are dispersed. Either the company reinvests the money or distributes a portion of the earnings to the stockholders. The value of investors and the market price of shares are both increased when corporate managers employ an effective framework of dividend decision, which is one of the fundamental principles of financial management. Share prices are heavily influenced by dividends, which are largely profit distributions to shareholders (McLaney, 1997). The dividend payout ratio and the amount of earnings retained by a company are directly related to the dividend choice made by the company, which is determined by the firm's dividend policy. With less money going out as dividends, the corporation will have more money to reinvest. Different factors, such as firm size, ownership, and other factors, influence the dividend decision. Investment prospects, profitability, regulatory constraints, liquidity, control, and inflation are just few of the many elements that go into deciding on a dividend policy in addition to the return on investment and the value of the company (Weston and Brigham, 1972). Income and expansion are crucial to the dividend decision (Adelegan, 2008).

DIVIDEND POLICY

In exchange for their investment in the company's stock, shareholders receive a dividend equal to a portion of the company's profits. A company's dividend policy is the set of rules for paying dividends established by the board of directors. The company's dividend policy should be so well-defined and consistently applied that every payout choice may be taken as an indicator of the company's long-term financial viability.

DETERMINANTS OF DIVIDEND POLICY

In the company, framing an appropriate dividend policy is the most challenging function of the management. The determinants of dividend policy are explained below,

a. Stable earnings

Stability in earnings is one of the key factors in influencing the dividend policy. The stable earnings of a firm performs better and slightly to pay out a higher proportion of its earnings as dividends.

b. Liquidity

Any company's ability to pay dividends is heavily dependent on its liquidity position. Although it is common to say that dividends are paid "out of earnings," Guthmann and dougall argue that a cash dividend can only be paid from available funds. The ability of a company to pay a cash dividend is determined in part by its financial status, including its cash on hand and its working capital. Investment and financing choices determine a company's liquidity and cash position, and dividend payments mean a cash flow.

c. Past Dividend

Existing companies often base their dividend payout percentage on the amount of dividends paid out in the years prior. Keeping the dividend rate constant is preferable from a practical standpoint.

d. Growth

Another important consideration for setting the dividend rate is the company's need for expansion. Dividends can be declared at a higher rate for a firm that has already expanded, but it is more difficult for a corporation in this position to grow its business.

e. Legal Restrictions

The rules and regulations of the law inform a company's dividend policy. Dividend payments are restricted to either current profits or historical gains once depreciation has been taken into account, per section 123 of the Indian Companies Act of 2013. Before dividends can be paid out, any losses from prior years must be offset against profits in the current year.

NSE NIFTY INDEX

National Stock Exchange index Ltd owns and operates the NIFTY fifty. It has been trading since April 21, 1996, making it a prime candidate for use in benchmarking, index funds, and index-based derivatives. There are several important parts of the Indian economy included in the Nifty Fifty Index. The report depicts the 50 most actively traded equity stocks on the stock exchange, out of a total of 1600 stocks. Information technology, financial services, consumer goods, entertainment and media, metal, pharmaceutical, communications, cement and its products, autos, pesticides and fertilizers, energy, and other services are just some of the 12 industries represented in the stocks.

Financial Sector

Both established providers of financial services in India are seeing fast growth, and new entrants are flooding the market. Commercial banks, insurance firms, non-bank financial institutions, cooperatives, pension funds, mutual funds, and other smaller financial supporting businesses are all included in this sector. India's government has implemented numerous reforms intended to open up, streamline, and improve the country's financial system.

Automobile Sector

India has moved up the ranks to become the fourth largest automaker and seventh largest producer of commercial vehicles in the world. The value of the Indian auto market is predicted to rise to between Rs.16.19 and Rs.18.19 trillion by 2026. The government's long-term goal is to make India a hub for manufacturing and R&D on a global scale. By 2023, India's government anticipates receiving $9 billion to $10 billion in foreign investment in the vehicle business.

Energy Sector

There is a wide range of enterprises in the energy sector that are all connected in some way. Investments in R&D are also a significant expense for the energy industry. The energy industry encompasses a wide range of interconnected businesses. Companies in the energy sector invest heavily on capital expenditures and have extensive fixed asset holdings.

FINANCIAL MARKET

One of the most trusted names in the world of finance opines that a "Financial Market" is any marketplace where buyers and sellers engage in the exchange of financial assets such as stocks, bonds, derivatives, and currencies. Transparent pricing, fundamental laws on trading, expenses, and fees, and market forces determining the values of assets that trade are all characteristics commonly associated with well-functioning financial markets.

Functions of Financial Market

Financial markets play an important role in the allocation of scarce resources in an economy by performing the following four important functions.

1. Mobilisation of Savings and channelling them into the most Productive Uses:

A financial market facilitates the transfer of savings from savers to investors. It gives savers the choice of different investments and thus helps to channelize surplus funds into the most productive use.

2. Facilitating Price Discovery:

Demand and supply work together to determine a product's selling price in the marketplace. Households act as the market's supply of money, while commercial enterprises stand in for the market's demand. The two of them interacting sets a price for the financial asset being traded.

3. Providing Liquidity to Financial Assets:

By allowing for a streamlined buying and selling process, financial markets increase the liquid value of financial assets, making it simpler to turn such assets into cash when needed. The mechanism of the financial market makes it easy for holders to sell their financial assets.

4. Reducing the Cost of Transactions:

Traded-in securities data is a key source of market intelligence for investors. Buyers and sellers of a financial asset can save time, energy, and money by using this service. In this sense, the financial market serves as a meeting place for people to exchange goods and services in order to satisfy their particular requirements. The financial markets are categorized according to the maturity of the financial instruments traded there. The money market is a financial exchange for short-term, liquid instruments with a maturity of less than a year. The capital market is used for the trading of long-term instruments.

CAPITAL MARKET

Capital markets allow individuals and organizations to trade financial securities, as defined by Investopedia, one of the most trusted online resources for financial information. Securities sales in the capital markets are a common way for both public and private organisations to raise money. Thus, both primary and secondary markets are included in this category. Investopedia notes that in order to run its own operations and make its own long-term investments, every government or corporation will need capital (funds). A corporation does this by issuing and selling its own stocks and bonds to the general public in exchange for monetary investment. The stock and bond markets are where these transactions take place. The savings of individuals are channeled into long-term productive investments via the Capital Market. Companies and governments alike can use the capital markets to raise funds for investments with a longer time horizon. Loans and stock sales are used to raise the funds. There are two distinct varieties of capital markets: The primary market is where newly issued securities are sold, whereas the secondary market is where previously issued securities are bought and sold. The Capital Market has a crucial role in fostering and maintaining economic progress, as stated in the Investors' Guide to the Capital Market (June, 2010), Investor Education and Protection Fund, Ministry of Corporate Affairs, Government of India. Important and successful, it serves as a medium for the mobilization and distribution of capital to businesses and as a catalyst for monetary investment. It is essential in encouraging people to put their money away in order to build up a country's economy over time. As a result, it plays a pivotal role in reshaping the economy into a dynamic sector that can better compete on the international stage through increased productivity, creativity, and efficiency.

Characteristics of Capital Market

Hiran Barua Avi defines the capital market as the place where companies can acquire the instruments that will be used to satisfy their long-term funding needs. Financial markets are a vast network of institutions and mechanisms that enable businesses, governments, and individuals to have access to both short-term and long-term financing. The monies are collected through transferable instruments that are already issued.

Characteristics

The following are the characteristics of a capital market:

1. Link between Savers and Investment Opportunities:

Capital market is a crucial link between saving and investment process. The capital market transfers money from savers to entrepreneurial borrowers.

2. Deals in Long Term Investment:

Capital market provides funds for long and medium term. It does not deal with channelizing saving for less than one year.

3. Utilizes Intermediaries:

Brokers, underwriters, depositories, and others serve as intermediaries in the capital market. Financial market intermediaries play a crucial role as the "blood vessels" of the market.

4. Determinant of Capital Formation:

The pace at which a country's economy creates new capital is determined by the actions of its capital market. Affluent people are encouraged to save more and invest more of their money in the capital market because of the lucrative returns they can get on their investments.

5. Government Rules and Regulations:

The capital market is unrestricted, yet it does take policy directives from the government into consideration. These markets are regulated by the government and operate under its guidelines. Capital markets should be ones in which all of the following conditions hold true: investors have access to adequate information; capital is allocated in a way that promotes growth; market operations are free, fair, competitive, and transparent; and capital is used in a productive manner.

Capital Market Instruments

According to the Securities and Exchange Commission, Nigeria the major instruments traded in the capital markets are medium and longer-term in maturity are discussed below:

1. Debt Instruments

To finance initiatives that require a large initial investment, debt instruments are often used. Both the primary and secondary markets offer opportunities to acquire it. Borrower ownership in this instrument-creditor arrangement does not indicate any stake in the firm being financed. Interest is due at regular intervals for the length of the contract, as indicated in the trust deed (contract agreement). Thus, the principle amount invested is returned at the end of the contract time, with interest paid quarterly, semiannually, or annually. The range ranges from three to twenty-five years. Because there is no inherent danger in investing in this instrument, the returns are lower than those offered by other securities on the capital market. These investors would rather see a company liquidated than continue operating. A bond issued by the federal government is known as a Sovereign Bond, while those issued by the states and municipalities are known as State Bonds and Municipal Bonds, respectively. When issued by a corporation, it is known as a Debenture, Industrial Loan, or Corporate Bond.

2. Equities (also called Common Stock)

In exchange for capital, the investor gains equity in the company and the right to sell it on the secondary market. An investor's rights and privileges may include the ability to vote on important company matters. Dividends are paid to the owners who hold equity in a company. This instrument carries a great degree of peril, but it also offers a substantial payoff. However, in the case of a company's liquidation, the owners would be paid out last.

CONCLUSION

This paper aimed to examine the impact of dividend policy on the profitability and share price of NIFTY firms from 2004-05 to 2018-19 and to determine the factors impacting dividend policy. Research into the factors that affect dividend policy shows that dividends have a significant impact on the dividend policies of the finance, energy, information technology, and metals industries. Increased investment yields growth potential, as seen in the automotive and pharmaceutical industries over the research period, which in turn has a significant impact on dividend policy. The potential for the metal and IT industries to increase their profitability. Financial sector dividend yield ratio was found to have a statistically significant positive effect on profitability over the study period, whereas dividend payout ratio was found to have a statistically significant negative effect on ROA and ROCE. When looking at the impact of dividend policy on profits in the auto and energy industries, we find that dividend yield ratios have a favorable impact, but dividend payout ratios have a negative impact. Profitability in the energy and pharmaceutical industries is positively correlated with the dividend yield ratio, whereas the pharmaceutical industry's dividend yield ratio was unrelated to its return on capital employed. When it comes to the information technology industry, dividend policy has been shown to reduce ROE and ROIC. The metal industry's dividend payment ratio has a favorable effect on share price, according to an analysis of the relationship between dividend policy and stock price.

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