



A STUDY ON DIVIDEND POLICY AND ITS EFFECT ON SHAREHOLDER VALUE AND FIRM PERFORMANCE

¹Mr. M. NABIRASOOL, ²KIRAN KALURI

¹Assistant Professor, ²MBA Student

Department of MBA

SVR Engineering College, NANDYAL

ABSTRACT

Dividend policy is an important financial decision that determines the proportion of profits distributed to shareholders and the portion retained for future growth. The main objective of this study is to analyze the impact of dividend policy on shareholder value and firm performance. Dividend decisions play a significant role in influencing investor confidence, market value of shares, and the overall financial stability of an organization.

This study examines how different dividend policies, such as high dividend payout, low payout, and retained earnings strategies, affect the financial performance of firms and the wealth of shareholders. The research focuses on key financial indicators such as profitability, earnings per share, return on equity, and market value to understand the relationship between dividend distribution and corporate performance.

The study is based on secondary data collected from financial reports, journals, and other relevant sources. Analytical methods are used to evaluate how dividend policy contributes to maximizing shareholder wealth and improving firm performance. The findings of the study highlight that a well-structured dividend policy can enhance investor satisfaction, maintain market reputation, and support sustainable financial growth.

The research concludes that dividend policy plays a crucial role in balancing the interests of shareholders and the long-term development of firms. Proper dividend decisions help companies maintain financial stability while creating value for shareholders.

I. INTRODUCTION

Dividend decision is one of the most important financial decisions taken by a firm because it directly affects shareholders' wealth and the long-term growth of the company. It deals with the choice of how much of the earnings should be distributed to shareholders as dividends and how much should be retained for reinvestment. This decision is closely related to investment and financing decisions, as retained earnings are an important and cost-effective source of finance. Therefore, the dividend policy of a firm plays a key role in determining its profitability, liquidity, market value, and overall financial performance.

Different firms follow different dividend policies depending on their financial position, growth opportunities, cash flow stability, and shareholder expectations. Some firms prefer a

stable dividend policy to build investor confidence, while others adopt a residual dividend policy to maximize reinvestment and future expansion. The relevance of dividend decisions has been widely debated in financial management through various theories such as dividend relevance theory, dividend irrelevance theory, bird-in-the-hand theory, and signaling theory. These theories explain how dividend payments may influence the market value of shares and investor behavior.

Firm performance is generally measured using indicators like profitability, return on assets, return on equity, earnings per share, and market value. Dividend decisions can influence these performance measures by affecting the firm's capital structure, cost of capital, and availability of internal funds. A well-planned dividend policy can enhance



shareholder satisfaction, improve market reputation, and attract potential investors, whereas an inappropriate policy may lead to liquidity problems and reduced growth opportunities.

In the present competitive business environment, companies must maintain a balance between rewarding shareholders and retaining sufficient earnings for expansion and risk management. Hence, an analytical study of dividend decisions and their influence on firm performance is essential to understand how dividend policies impact financial efficiency and shareholder value. This study helps investors, financial managers, and policy makers to make informed decisions regarding dividend distribution and corporate financial planning.

NEED OF THE STUDY

The study of dividend decisions and their influence on firm performance is important because dividend policy directly affects both shareholders' income and the financial stability of a company. Investors often consider dividend payments as a sign of profitability and future growth, while firms must ensure that dividend distribution does not reduce funds required for expansion and operational needs. Understanding this relationship helps in evaluating whether higher dividends improve market value or limit reinvestment opportunities. This study is needed to analyze how dividend payouts impact key performance indicators such as profitability, return on equity, earnings per share, and liquidity. It also helps to identify whether firms with stable dividend policies perform better than those with irregular or low dividend payments. The findings will support financial managers in designing an optimal dividend policy that balances shareholder expectations and long-term growth. Moreover, it provides useful insights for investors in making better investment decisions based on dividend behavior and firm performance.

OBJECTIVES OF THE STUDY

- To examine the relationship between dividend payout ratios and firm

performance indicators such as Return on Assets (ROA), Return on Equity (ROE), and Earnings per Share (EPS) across selected firms.

- To analyze how dividend stability and changes in dividend policy influence market valuation measures, including stock price performance and firm value (Tobin's Q).
- To evaluate the applicability of dividend theories—such as dividend relevance, irrelevance, signaling, and agency cost theories—in explaining observed corporate performance outcomes.
- To assess the impact of firm-specific factors (profitability, leverage, liquidity, growth opportunities) on dividend decisions and their subsequent effect on financial performance.
- To provide empirical recommendations for corporate managers and investors regarding optimal dividend policies that enhance sustainable firm performance and shareholder wealth.

SCOPE OF THE STUDY

The scope of the study focuses on analyzing dividend decisions and their impact on the financial performance of selected firms. It examines different dividend policies such as stable dividend, residual dividend, and payout ratio, and evaluates how these policies influence profitability, return on assets, return on equity, and earnings per share. The study covers the relationship between dividend payments and firm value, shareholder wealth, and internal financing capacity. The analysis is limited to secondary financial data collected from annual reports and financial statements of selected companies for a specific period. It considers only measurable financial indicators to assess firm performance and does not include qualitative factors such as management strategy or investor psychology. The study is useful for understanding how dividend decisions affect financial efficiency and market performance within the chosen sample. The results provide insights for investors, financial managers, and researchers



regarding the role of dividend policy in corporate financial management and decision-making.

II. RESEARCH METHODOLOGY

This analytical study examines dividend decisions and their influence on firm performance. It investigates how dividend payout policies affect profitability, market value, and shareholder wealth. The research adopts a quantitative approach, using financial data analysis to evaluate relationships between dividend patterns and key performance indicators of selected firms.

Primary Data

Primary data will be collected through structured questionnaires distributed to financial managers, investors, and company executives. Interviews may also be conducted to understand managerial perspectives on dividend decisions, policy formulation, and their perceived impact on company performance and shareholder value.

Secondary Data

Secondary data will be gathered from annual reports, financial statements, stock exchange records, company publications, and academic journals. Published research articles, books, and financial databases will also be used to analyze dividend payout ratios, earnings trends, and firm performance indicators.

Sampling Method

Companies will be categorized into sectors (such as manufacturing, services, and finance). From each sector, firms will be randomly selected to ensure fair representation and reduce sampling bias.

Sample Size

The study will include (financial managers, executives, and investors) selected from the chosen firms.

LIMITATIONS OF THE STUDY

- The study is based only on selected companies, so findings may not represent the dividend behavior of all industries or firms.
- The analysis uses secondary data from financial statements, which may

contain reporting errors and limit the accuracy of performance evaluation.

- The study covers a limited time period, which may not reflect long-term dividend policy trends and their impact on firm performance.
- Only quantitative financial indicators are considered, ignoring qualitative factors like management decisions, market conditions, and investor sentiment influencing dividends.
- External economic factors such as inflation, interest rates, and policy changes are not included, which may affect dividend decisions and performance.

III. LITERATURE SURVEY

N. Shwetha (2025) The Dividend Decision, in corporate finance, is a decision made by the directors of a company. It relates to the amount and timing of any cash payments made to the company's stockholders. The decision is an important one for the firm as it may influence its capital structure and stock price. In addition, the decision may determine the amount of taxation that stockholders pay. There are three main factors that may influence a firm's dividend decision: Free-cash flow Dividend clientele Information signaling The free cash flow theory of dividends Under this theory, the dividend decision is very simple. The firm simply pays out, as dividends, any cash that is surplus after it invests in all available positive net present value projects. A key criticism of this theory is that it does not explain the observed dividend policies of real-world companies. Most companies pay relatively consistent dividends from one year to the next and managers tend to prefer to pay a steadily increasing dividend rather than paying a dividend that fluctuates dramatically from one year to the next. These criticisms have led to the development of other models that seek to explain the dividend decision. Dividend clientele A particular pattern of dividend payments may suit one type of stock holder more than another. A



retiree may prefer to invest in a firm that provides a consistently high dividend yield, whereas a person with a high income from employment may prefer to avoid dividends due to their high marginal tax rate on income. If clienteles exist for particular patterns of dividend payments, a firm may be able to maximize its stock price and minimize its cost of capital by catering to a particular clientele. This model may help to explain the relatively consistent dividend policies followed by most listed companies. A key criticism of the idea of dividend clienteles is that investors do not need to rely upon the firm to provide the pattern of cash flows that they desire. An investor who would like to receive some cash from their investment always has the option of selling a portion of their holding. This argument is even more cogent in recent times, with the advent of very low-cost discount stockbrokers. It remains possible that there are taxation-based clienteles for certain types of dividend policies. Information signaling A model developed by Merton Miller and Kevin Rock in 1985 suggests that dividend announcements convey information to investors regarding the firm's future prospects.

Penn Collins (2024) This study is aimed at examining the effects of dividend policy on the capital structure of firms. Linear regression is carried out via a three-stage triple least square method using secondary data on a sample of 444 firms. The results show that dividend policy has a negative effect on capital structure and consequently when dividend increases the level of debt falls. On the other hand, capital structure has a positive effect on dividend policy implying that when a firm resort to debt it pays more dividends. However, the results are not the same in all the sectors of activity. In the primary sector, capital structure is influenced by financial profitability liquidity, size, tangibility of assets, asset growth, cash flow and tax. In the secondary sector, capital structure is negatively affected by dividend policy and positively by size. While in the tertiary sector,

capital structure is significantly influenced by dividend policy.

Dr. Obayagbona (2024) Dividend policy, a critical decision for listed companies, involves determining the allocation of profits for retention or distribution as dividends to shareholders. This decision hinges on dynamics such as liquidity and investment prospects. The business performance of companies serves as a pivotal indicator of their sustainability, capturing the interest of investors. This study aimed to assess the impact of dividend policy on Nigerian consumer goods companies, specifically examining the effects of dividend payout, dividend yield, and firm size on financial performance. The study population comprised 169 companies listed on the Nigerian Stock Exchange as of December 31, 2022, with a sample of six companies analyzed over a ten-year period (2012-2021). The findings indicate that dividend payout, dividend yield, and firm size exerted a positive and significant influence on return on assets, while firm liquidity demonstrated a substantial adverse influence on the financial performance of consumer goods companies in Nigeria during the investigation period.

Dewa Gede Wirama (2024) Using the residual dividend theory, this study examines the impact of capital expenditures and working capital on the dividend policies of publicly listed companies in Indonesia. Using data on public companies (other than those in the financial sector) listed on the Indonesia Stock Exchange from 2011 to 2020, this study collected 870 observations (firm-years). This study employs a regression analysis technique using the STATA application program. The main variables in this study are capital expenditure and working capital, and the control variables are sales growth, firm size, leverage, profitability, liquidity and dummy variables for state-owned enterprises. The dependent variable of dividend policy is proxied by the dividend payout ratio.

Salwa Said (2024) Corporate dividend policy is one of the most challenging issues in the



corporate finance field. The decision of dividend policy is considered an important managerial decision as it could have a serious impact on firm performance and firm value. Many researchers have investigated the association between dividend policy and firm performance in different countries and contexts. Different theories and a large body of theoretical and empirical literature have addressed the relationship between dividend policy and firm performance, yet there is no consensus on this issue, and the debate on dividend policy is still open. This study aims to present a comprehensive review of theories and empirical literature concerning the association between corporate dividend policy and its performance for more explanation and understanding of this important topic. This study contributes to corporate dividend policy literature by identifying the potential gaps in previous literature and presenting suggestions for further research.

IV. FINDINGS, SUGGESTION AND CONCLUSION

FINDINGS

- Axis Bank showed the strongest and most consistent growth in EPS and ROE, indicating high profitability and efficient use of shareholders' funds.
- Exide Industries maintained high earnings and the highest ROE overall, though its performance fluctuated in 2024 before recovering in 2025.
- ICICI Bank demonstrated steady improvement in ROE and EPS until 2024, but EPS declined sharply in 2025 due to equity expansion and earnings dilution.
- Union Bank recorded the lowest EPS and ROE throughout the period, reflecting weak profitability and inefficient utilization of equity capital.
- Dividend yield was highest in ICICI Bank from 2021 to 2024, while Axis Bank showed stable and improving dividend returns, reaching the highest yield in 2025.

- Exide Industries maintained the lowest dividend yield, indicating a retention-oriented policy for future growth.
- Union Bank's dividend policy was unstable, with sharp reductions during low-profit years and only partial recovery later.
- P/E ratios indicate that Axis Bank remained relatively undervalued despite strong earnings, while Exide Industries had higher market valuation.
- ICICI Bank's P/E increased sharply in 2025 due to lower EPS and higher market price, showing valuation pressure.
- Walter's model suggests Exide Industries and Axis Bank are growth firms ($r > k$), favoring profit retention, while ICICI Bank tends toward higher dividend payout ($r < k$).
- Union Bank requires a balanced dividend policy due to unstable earnings and limited growth opportunities.
- Overall, firms with stable earnings and balanced dividend policies showed better financial performance and higher shareholder value.

SUGGESTIONS

- Companies should maintain a stable and consistent dividend policy to build investor confidence and improve market valuation.
- Growth firms like Axis Bank and Exide Industries should retain a higher portion of earnings since their internal rate of return is greater than the cost of capital.
- ICICI Bank should follow a balanced dividend policy, ensuring adequate payout while controlling equity dilution to protect EPS.
- Union Bank should focus on improving profitability and operational efficiency before increasing dividend payments.



- Firms should align dividend decisions with earnings stability rather than market price fluctuations.
- Management should regularly evaluate the relationship between return on equity and dividend payout to maximize shareholder value.
- Companies should avoid excessive dividend distribution that may reduce retained earnings required for future expansion.
- Financial performance indicators like EPS and ROE should be strengthened to support sustainable dividend growth.
- Investors should consider both dividend yield and profitability ratios before making investment decisions.
- Firms should adopt an optimal dividend policy based on Walter's model by comparing internal return with cost of capital.
- Regular monitoring of capital structure and cost of equity will help in making effective dividend decisions.
- Companies with unstable earnings should adopt a conservative dividend policy to maintain financial stability and long-term growth.

CONCLUSION

The study on dividend decisions and their influence on firm performance highlights the important role that dividend policy plays in financial management and shareholder value. Dividend decisions are not only related to the distribution of profits but also reflect the financial strength, growth prospects, and stability of a firm. A well-structured dividend policy helps in maintaining investor confidence, improving market reputation, and attracting potential shareholders, which ultimately contributes to the enhancement of firm value.

The analysis shows that there is a significant relationship between dividend payments and key performance indicators such as profitability, return on equity, earnings per

share, and liquidity. Firms that maintain a stable and consistent dividend policy tend to perform better in terms of financial stability and market valuation, as regular dividends signal strong financial health and efficient management. At the same time, excessive dividend payouts may reduce retained earnings and limit funds available for future investment and expansion. Therefore, firms must maintain a proper balance between dividend distribution and profit retention to ensure sustainable growth.

The study also confirms that dividend policy influences investor perception and investment decisions. Investors often prefer firms with predictable dividend patterns, as it reduces uncertainty and provides regular income. However, growth-oriented firms may prefer lower dividend payouts to finance new projects and maximize long-term returns. Hence, the optimal dividend policy depends on the firm's financial position, growth opportunities, and shareholder expectations.

In conclusion, dividend decisions have a measurable impact on firm performance and shareholder wealth. A balanced and consistent dividend policy supports financial stability, enhances market value, and ensures long-term growth. The findings of this study are useful for financial managers in designing effective dividend strategies and for investors in making informed investment decisions based on dividend behavior and company performance.

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