

Dividends, Wealth Effects and Forecasting Return Volatility

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Abstract

The study presents a novel evidence to evaluate wealth effects due to dividends, with integration of firm size and volatility modelling through GARCH (1, 1) model. Shareholders' wealth effects across short-run, medium-run and long-run have been examined. The present study uses a sample of 77 Indian Healthcare and Pharmaceutical firms with a total of 555 final cash dividend announcements spread across 2005 to 2015. Research design involves event study applying combination of statistical and economic models to ascertain an event impact's direction, timing and magnitude. The results indicate strong support for dividend information content with impact's direction and magnitude being sensitive to timing horizon and firm size. In short -run irrespective of firm size wealth creation is revealed. Significant positive abnormal returns for small cap and large cap advocates respectively for long term and short term wealth creation.

JEL Code : G1, G10, G14, G17, G35

Keywords : Dividends, volatility models, stock market reaction, shareholders' wealth, wealth effects

I. Introduction

UNDERSTANDING THE DIVIDENDS' impact on wealth effects and forecasting volatility in returns is essential for analysts and investors. It elucidates the complex connections between dividend policies and market behaviour.

The information content hypothesis reflects the influence on market prices once a new information is floated in the market. The dividend information content acts as a fundamental estimator, driving the perceived behaviour of a market due to dividend announcements. Also, asymmetric

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Study reports greater magnitude (4.7006% for DA and 12.7950% for DASC) of positive and significant CAAR in long-run compared to short and medium-run. This infers for better wealth creation opportunities by holding dividend announcing firm's share for at least a year. Also, dividend announcing small cap firms would be prime pick for the investors preferring holding the investment and not regularly churning the portfolio. While dividend paying large cap firms provide best wealth creation opportunities in medium-run and the same reduces in holding the share beyond two months from the date of announcements. Hence, it can be more appropriate for investors not reluctant to regularly churn the portfolio for better growth opportunities. The findings of ICD for MC only matches with the negative information content hypothesis of dividend. Past volatility can be used to forecast future volatility in returns for dividends by small-cap firms only. The results of presence, direction and magnitude of dividend information impact, on Indian stock market with volatility modelling, clarifies the anomaly regarding wealth generation opportunities in India. The present study opens two new areas for future research mainly comparing ICD with respect to incorporation of pattern of dividend for each firm size. A study can also be extended with a comparative analysis of same industry of emerging and developed economies.

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Appendix I Event Sample Construction

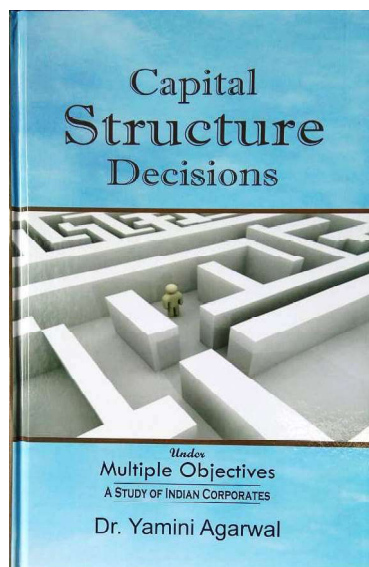
Dividend Announcements (DA) during 2005 to 2015	# of Firms	# of Dividend Announcements
Total Cash Dividend Announcements (Including interim, quarterly, special and final dividends)	99	909
Less: Total interim, quarterly and special Dividend Announcements		175
Less: Suspended/ Delisted Firms and Firms with onetime final dividend announcements in last 10 years	22	179
Total Final Cash Dividend Announcements Sample	77	555
Group - A : All Dividend Announcements	77	555
Group - A.1: Dividend Announcements on the basis of Firm size* (DABFZ)	77	555
Dividend Announcements by Large Cap firms (DALC)		65
Dividend Announcements by Mid Cap firms (DAMC)		73
Dividend Announcements by Small Cap firms (DASC)		417

Notes: * Previous researches have often taken firm size as a proxy for information asymmetry (McLaughlin et al., 1998, Acker, 1999 and Haw and Kim, 2016). Dividend sample categorization of Healthcare & Pharmaceutical firms, based on firm size, is performed using the large-cap, mid-cap and small-cap classification defined as per Securities and Exchange board of India (SEBI) (2017) circular. For details please see, SEBI circular (2017) categorization and Rationalisation of Mutual Fund Schemes.

Appendix II Sample summary statistics and year wise frequency of Dividends for Group - A and A.1

Sample	Group - A : All Dividend Announcements (DA)	Group - A.1 : Dividend Announcements based on Firm Size (DABFS)		
		Large Cap	Mid Cap	Small Cap
Subsample				
No. of Firms	77	7	9	61
Years				
2006	51	7	6	38
2007	46	6	4	36
2008	60	7	7	46
2009	60	7	7	46
2010	61	7	8	46
2011	63	7	8	48
2012	51	6	8	37
2013	57	6	9	42
2014	52	6	9	37
2015	54	6	7	41
Sample Size	555	65	73	417
%	100	12	13	75
Mean Frequency per firm	7.21	9.29	8.11	6.84
Mean	56	7	7	42
Mode	51	7	7	46
Maximum	63	7	9	48
Minimum	46	6	4	36
Standard Deviation (SD)	5.24	0.50	1.42	4.31

Source : Compiled from Websites of BSE India and Economic Times



Capital Structure Decisions under Multiple Objectives : A Study of India Corporates

Contents

- Literature Review & Synthesis
- Research Methodology
- Understanding of Capital Structure Practices in India
- Capital Structure Decisions : A Case of Multiple Objectives
- Capital Structure Decisions under Multiple Objectives : Application & Testing of the Model
- Summary and Conclusion
- References
- Appendices

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