Impact of Dividend Announcements on the Stock Prices and Liquidity: Evidence from India

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Abstract

Dividend is the rate of return earned by the investors on their investment and consistent dividend payments have spillover effects on the stock prices. Many researches reveal that the dividend announcements convey positive information about the company and hence make a positive impact on the stock prices. Also very few studies analyzed the impact of dividends on trading volume but none of them gave any conclusions regarding the liquidity in the post announcement period. By using daily stock prices and stock trading volume the present study tries to find out an evidence of whether announcement of dividend has any effect on the stock prices and also on the stock liquidity. For the purpose of conducting the study dividends announced annually by 50 companies forming part of NIFTY 50 index of National Stock Exchange (NSE), India was selected. The study used the annual dividends announced by the companies for a period between January 2011 to December 2015. Using the Market Model of Event Study Methodology it was found that though the dividend announcement had a significant impact on both the stock prices as well as on the stock trading volume but a long term positive impact was recognized in case of stock prices. This suggested that dividends do signal positive information about the company and thereby drive the stock prices higher leading to abnormal gains to the traders. With respect to stock liquidity, it was concluded that the trading volume had a short term significant decrease on account of dividend announcement and hence resulted into a lower liquidity in the post announcement period.

Key Words: Dividends, Stock Prices, Event Study, Liquidity, Average Abnormal Return, Cumulative Average Abnormal Return (CAAR)

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