EFFECTS OF DIVIDEND POLICY ON SHARE PRICES:
A CASE STUDY OF COMPANIES LISTED IN THE NAIROBI
SECURITIES EXCHANGE

BY

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UNITED STATES INTERNATIONAL UNIVERSITY AFRICA

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STUDENT’S DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University in Nairobi for academic credit.

Signed: ________________________________ Date: __________________
Michael Muturi Ndungu (ID 617925)

This project has been presented for examination with my approval as the appointed supervisor.

Signed: ________________________________ Date: __________________
Marion Mbogo

Signed: ________________________________ Date: __________________
Dean, Chandaria School of business
ABSTRACT

The aim of this study was to determine the effects of dividend policy on market share prices, with a special reference to companies listed in the Nairobi Stock Exchange. This was in reference to the following specific objectives; to investigate the considerations made by companies before announcement of dividends; to investigate the reaction of share market prices to dividend announcements and to examine the effects that dividend payout ratio has on share prices.

This study adopted a descriptive research design. The study targeted a population of 59 firms quoted at the Nairobi Securities Exchange (N.S.E). A sample of 30 firms was selected consisting of all the firms quoted consistently at N.S.E for a period of 5 years from 2007 – 2011. A period of 5 years was chosen because the researcher considered the period to be adequate for establishing any relationship between dividend payout ratio and the value of the firm as reflected in the share prices and the secondary sources obtained from the companies’ financial records from N.S.E. The data collection tool used in this study was the desk data collection. Data collected from documentary review was analyzed using simple linear regression and correlation analysis.

The study found out that companies consider several issues before issuing dividends which include dividends paid in the previous period, the dividends to be given to the preferred shareholder, what the rival companies pay, the net earnings during the period, the amount in the reserves and the investment prospects. It also concludes that the share market is positively responsive to the dividend announcement such that the share market value of dividends improves in the few weeks after a high dividends announcement. This is consistent with several previous studies thus pointing to the fact that there is information content associated with dividends. The study recommends that companies should consider all pertinent issues before issuing dividends.

The study findings depicted that share prices have a positive significant relationship with the announcement of the company’s dividend payout ratio. Therefore, when a firm declares positive news or negative news to the public the information is quickly adjusted on the share prices. The findings are in tandem with the efficient market hypothesis theory which postulates
that whenever positive news are declared publicly then the share price must increase and vice versa.

The study concludes that there is a positive significant relationship between the dividend announcement and the share price. Since the share market is positively responsive to the dividend announcement, companies should always strive to pay divided consistently for their shares to perform well at the stock exchange. Further, the study findings showed that there is a positive significant relationship between the payout ratio and the share price. The research also recommends that firms should maintain a clear and consistent dividend policy for the dividend policy to affect the value of the firm.

The study recommends that a similar study should also be done whereby the data collection relies on primary data i.e. in-depth questionnaires and interview guide so as to complement this study. Due to the shortcomings of regression models, other models can be used to explain the various relationships between dividends payout ratios and the value of the firms.
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DEDICATION

This study is dedicated to my loving family and friends
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Study

Dividends are per-share payments designated by company’s board of directors to be distributed among shareholders. For preferred shares, it is generally a fixed amount. For common shares, the dividend varies with the fortunes of the company and the amount of cash on hand. It may be omitted if the business is poor or the directors withhold earnings to invest in plant and equipment (Garver, 2011). Since most closely held companies do not pay dividends, when using dividend capitalization valuators must first determine dividend paying capacity of a business. Dividend paying capacity based on average net income and on average cash flow is used (Husseman, 2010).

To determine dividend paying capacity, near term capital needs, expansion plans, debt repayment, operation cushion, contractual requirements, past dividend paying history of a business and dividends of a comparable company should be investigated. After analyzing these factors, percentage of the net income of average cash flow that can be used for the payment of dividend can be estimated. What also must be determined is the dividend yield, which can best be determined by analyzing comparable companies. As with the price earnings ratio method, this usually produces a subjective result (Husseman, 2010).

The securities exchange is part of the securities segment of the capital market. Investments that represent evidence of debt, ownership of a business, or the legal right to acquire or sell an ownership interest in a business are called securities. The most common types of securities are stocks, bonds and options. Securities markets are the mechanisms that allow suppliers and demanders of funds to make transactions. They also allow transactions to be made quickly and at a fair price (N.S.E, 2007).

Dividends are relevant because they have informational value. Financial signaling theory implies that dividends may be used to convey information. Information, rather than dividends itself, affects share prices (Brigham and Gapenski, 2004). The payment of dividends conveys to shareholders that the company is profitable and financially strong.
This in turn causes an upsurge in demand for the firm’s shares causing a rise in their market prices.

When a firm changes its dividends policy, investors assume that it is in response to an expected change in the firm’s profitability which will last long. An increase in payout ratio signals to shareholders a permanent or long term increase in firm’s expected earnings. Accordingly, the prices of shares are affected by changes in dividends policy. This, therefore call for studies to be conducted in the area of dividend policy and how this policy affects market prices of shares (Husseman, 2010).

The Nairobi Securities Exchange which was formed in 1954 as a voluntary organization of stock brokers is now one of the most active capital markets in Africa. The administration of the Nairobi Securities Exchange Limited is located on Exchange Building, Westland’s Nairobi. As a capital market institution, the Securities Exchange plays an important role in the process of economic development. It helps mobilize domestic savings thereby bringing about the reallocation of financial resources from dormant to active agents.

Long-term investments are made liquid, as the transfer of securities between shareholders is facilitated. The Exchange has also enabled companies to engage local participation in their equity, thereby giving Kenyans a chance to own shares (N.S.E, 2007). A stock market is a place where securities are traded. These securities are issued by listed companies and by the government, with the aim of raising funds for different purposes such as to fund expansion for the former, and development and finance budget deficits for the latter. Common securities traded on a stock exchange include company shares, corporate bonds, and government debt in the form of treasury bonds (N.S.E, 2010).

Companies can also raise extra finance essential for expansion and development. To raise funds, a new issuer publishes a prospectus which gives all pertinent particulars about the operations and future prospects and states the price of the issue (Green, 1993). A stock market also enhances the inflow of international capital by directing capital to productive uses. The savers (governments, businesses, and people who save some portion of their income) invest their money in capital markets like stocks and bonds. The borrowers
(governments, businesses, and people who spend more than their income) borrow the savers’ investments that have been entrusted to the capital markets (Lonie, 1990).

These members of the NSE transact business mainly on the floor of Nairobi stock market which is in Exchange Building, Westland’s Nairobi, with a limited proportion of business conducted in foreign securities through overseas agents. The stockbrokers act as financial advisers to their clients and carry out their orders. The Nairobi Stock Exchange deals in both variable income securities and fixed income securities. Variable income securities are the ordinary shares, which have no fixed rate of dividend payable, as the dividend is dependent upon both the profitability of the company and what the board of directors decides. The fixed income securities include treasury and corporate bonds, preference shares, debenture stocks - these have a fixed rate of interest/dividend, which is not dependent on profitability (N.S.E, 2007).

According to Anyanzwa (2008), listing is the process of taking a privately owned organization and transforming it into a publicly owned entity whose securities (equity or debt) can be traded on a securities exchange. As at February 2015, there are 64 companies listed in NSE; agricultural 7, automobiles and accessories 3, banking 10, commercial and services 9, construction and allied 5, energy and petroleum 5, insurance 6, investment 3, investment services 1, manufacturing and allied 9, telecommunication and technology 1 and growth and enterprise segment 4. The stock market consists of both the primary and secondary markets. In the primary or new issue market, shares of stock are first brought to the market and sold to investors. In the secondary market, existing shares are traded among investors (Ross, Westerfield and Jaffe, 2003).

1.2 Statement of the Problem

In Kenya, most of the firms listed in the stock exchange pay dividends semiannually. There is no legal requirement that firms adopt a specific dividend policy schedule, however dividend distribution do face legal restrictions for instance they should not be paid out of capital unless liquidating. The dividends and dividend policy have been subject of many studies for many years from past to present (Lintner, 1956; Gordon, 1959; Miller and Modigliani, 2011; Mancinelli and Ozkan, 2006).
Karanja (2007) studied dividend practices of publicly quoted companies and found out that there are many reasons why firms pay dividends. One reason is lack of investment opportunities, which promises adequate returns. Firm’s cash position was the most important consideration of timing of dividends. Onyango (2009) noted that shareholders tend to receive higher cash dividends after bonus issue. Njoroge (2001) examined relationship between dividend payout and some financial ratios such as return on assets. The results obtained were that the most significant variable in making dividend decisions is return on assets while return on equity and growth in assets are not considered in making dividend decisions.

It has however remained a puzzle whether a company’s dividend policy really affect the firm’s share market prices. Some scholars argue that dividend policy is irrelevant (Miller and Modigliani, 2011) whereas others view it otherwise. Hence the study was set to determine whether there existed a causal relationship between dividend policy and the share prices of a firm. Since there is difficulty in linking dividend policy directly to share prices (NLI Research, 2006), this study aimed at filling the knowledge gap that exists in determining the effect of dividend policy on share prices.

1.3 General Objective

The objective of this study was to determine the effects of dividend policy on market share prices, with a special reference to companies listed in the Nairobi Securities Exchange (NSE).

1.4 Specific Objectives

1.4.1 To investigate the considerations made by companies listed in the NSE before announcement of dividends.
1.4.2 To investigate the reaction of share market prices to dividend announcements.
1.4.3 To examine the effects that dividend payout ratio has on share prices

1.5 Significance of the Study

Difficulties arise in trying to link dividend policy directly to share prices. Despite the clarity in the link between dividend policy and share prices, standard theory would lead us to only one conclusion that dividend policy has no effect on share price leaving little room to
discuss why dividend policy matters. The findings on the effect of dividend policy on market share prices will be invaluable to:

1.5.1 The Management of the Companies listed in the NSE
The management of quoted companies will be able to determine the effect of dividends on the share value of their firms so that they can make prudent decisions regarding dividend policies.

1.5.2 The Government
The government of Kenya will be enlightened in a bid to make policies relating to dividends taxes. The knowledge of the effect of dividends on the value of the firms will assist in ascertaining the appropriate amount of tax to pay for dividends paid out and their effects on value of the firm.

1.5.3 Financial Consultants
These findings will enable financial consultants to offer proper services e.g. financial advice to their clients. This relates to optimal dividend policy where the share value of their firms in the stock market can be maximized.

1.5.4 Scholars and Academicians
The study will be of help to scholars and academicians who may wish to use its findings as a basis for further research on this subject.

1.5.5 Investors
Investors who may need to know the relationship between dividends policy and share value of the firm for them to choose which firm to invest their funds in and as a result shun impetuous investment decisions.

1.6 Scope of the Study
This study was limited to Nairobi Securities Exchange and covered companies listed in N.S.E. Though currently there are 64 quoted companies the study was limited to 59 listed companies on the N.S.E as of December 2011. The study was limited to the to the 59 companies listed in the Nairobi Stoke Exchange because they provided current information
for the study and that the remaining companies had not declared or paid dividends for at least the last five years. There was also a challenge in finding consistent information on the dividends policies. To mitigate this limitation, the study focused on only those companies with consistent information. The researcher believed that this provided an adequate population and sample for the study therefore giving reliable results and findings for the period 2007-2009. The study concentrated on the dividend practice and its influence in prospect of listed companies in N.S.E. The limitation of the study was that data was taken from secondary sources. Further, the result and the interpretation are completely rigid and from the viewpoint of the researcher with only the cash element dividend being the only one taken for the analysis. To mitigate this, the researcher ensured that the accuracy of the information was achieved so that only the correct data was used in the study.

1.7 Definition of Terms

1.7.1 Dividend
Dividend is finance stockholder's share as profit: company profits paid pro-rata to stockholders, either in cash or in more shares (Brav, et al., 2005).

1.7.2 Dividend Policy
Dividend policy is the blueprint used to determine the fraction of the dividends to be shared and or reinvested (Arnott, 2003).

1.7.3 Share Price
Share price is the market value of the security in the free financial capital market for equity (Baker, 2001).

1.7.4 Liquidity
Liquidity is the degree to which an asset or security can be bought or sold in the market without affecting the asset’s price. Liquidity is characterized by a high level of trading activity (Bernstein, 2005).

1.8 Chapter Summary
The chapter takes into consideration the background of the problem under study laying out the statement of the problem clearly. The purpose of the study is outlined in the general
objective clause. The research questions depict the hypothesis under consideration and the specific objectives of the study. Justification is given for the reasons to undertake this study as opposed to any other. The scope of the study is stated so that the limitations can be noted clearly and terminologies are also explained towards the end of the chapter. The next chapters include; chapter two which focuses on the literature review done on the effects of dividend policy on share prices; chapter three which focuses on the research methodology and chapter four which presents the findings and the results of the study and chapter five which discusses the summary of the findings, the discussion of the findings, the conclusions and the recommendations.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This section analyses literature related to the effects of dividend policy on share prices. The main source of literature is past studies and a detailed study of the three objectives which include: to investigate the considerations made before announcement of dividends, to investigate the reaction of share market prices to dividend announcements and to examine the effects that dividend pay-out ratio has on share prices. It also includes a critical review of the literature, and a summary of the chapter.

2.2 Considerations Made Prior to Announcements of Dividends

It is argued that the announcement of changes in dividend policy influences the price of shares and that manager’s use the dividends changes to convey information about the future earnings of their companies (Bernstein, 2005). They may also influence the perceptions of the investors about the briskness of the company by following a stable dividend policy where the actual briskness of the company remains unchanged. This sort of argument is known as the dividend signaling hypothesis (Ross, 1989).

2.2.1 Changes in Management’s Announcement of a Firms Future Profitability

According to the dividend information content hypothesis, dividend changes trigger stock returns because they reflect changes in management’s announcement of a firm’s future profitability. This hypothesis has motivated a considerable amount of theoretical and empirical research (Modigliani and Miller, 1958).

The question of whether dividend announcements have any information content went through multiple stages. In its early stage, it was just of interest to test whether the market reacts to these announcements or not. The research conducted during this stage examined either dividend initiations or omissions (Asquith and Mullins, 1983; Healy & Palepu, 1988; Venkatesh, 1989) or the changes in dividends in general, (Aharoni and Swary, 1994; Woolridge, 1982; Eades, Hess and Kim, 1985).
According to Modigliani and Miller (1958), they accept the information content of dividend but contend that the price of the share is determined by the expected future earnings and the firm’s investment policy and not by the dividends. They argue that the informational value of dividends indicates that they are merely a reflection of the firm’s investment policy and the expected earnings and do not have any impact on the share prices in their own accord.

2.2.2 Changes in Dividends

There is an abundance of evidence associating announcements of changes in dividends with abnormal share price performance. This evidence indicates that the announcement of increases in dividends are associated with significant positive abnormal/excess returns and the announcement of decreases in dividends are associated with significant negative abnormal/excess returns while the announcement of no-changes in dividends produce only normal returns for shareholders. According to Faloye and Oluwole (2014), there is a significant positive relationship between dividend announcement and share price on a bullish market whereas bearish market registered a negative significant relationship. Moreover, the investors had consistent behavior if there were on the same market sector.

This market phenomenon is known as the dividend announcement effect. Researchers have examined the impact of dividend announcements on share prices from a variety of different perspectives and in a selection of different circumstances. For example, a number of researchers have investigated the market reaction to the announcement of changes in regular dividends paid to equities (Pettit, 1989; Charest, 1978; Aharony and Swary, 1994; Woolridge, 1982; Divecha and Morse, 1983).

Others have analyzed the market response to the announcement of major changes in a firm’s dividend policy such as dividend initiations and/or omissions (Pettit, 1989; Asquith and Mullins, 1983; Benartzi, Michaely and Thaler, (2007); Dielman and Oppenheimer 1984). A related research area concentrates on the announcement of special as opposed to regular dividends (Brickley, 1983). Academics have also considered the consequences of a dividend announcement on trading volume patterns (Richardson, Sefcik and Thompson, 2006). Share price volatility (Venkatesh, 1989), the revision of analysts’ forecasts and the speed of any associated price adjustment (Patell and Wolfson, 1984).
Three main theoretical arguments have been proposed to justify the market response to dividend announcements observed in the above studies. First, in a world of information asymmetry, where managers have access to detailed internal reports with data relating to the profitability of the firm, alterations in dividend policy convey managerial assessments of future profitability/cash flows of the firms to the outside investors (Bhattacharya, 1979).

This argument was recognized by Miller and Modigliani (1958) even though they proposed that no relationship should exist between the dividend policy and the market value of the firm; they admitted that “where a firm has adopted a policy of dividend stabilization with a long-established and generally appreciated target payout ratio, investors are likely to (and hence have good reason to) interpret a change in the dividend rate as a change in the management's view of the future profit prospects of the firm” (Miller and Modigliani, 1958). In this context, dividend increases (decreases) convey favorable (unfavorable) information about current and future profitability of firms to the outside investment community.

Second, managers may disclose information about their policy for financing investments to the market through dividend decisions (Keane, 1985); according to this view, a high dividend payout policy is associated with new equity/debt financing while a low dividend payout policy is associated with the financing of capital expenditure through retained earnings (Fazzari, Hubard & Petersen, 1988; Lonie, Power & Sinclair, 2005; Garver and Garver, 1993). Investors may prefer the former combination because a large quantity of information is usually disclosed about the proposed investment in the share prospectus; uncertainty is reduced in comparison to the situation where most of the information about the investment remains undisclosed. Jensen (1988) strengthens this argument advocating that companies should adopt a high dividend payout strategy, stripping managers of their liquid assets and sharply reducing their capacity for independent decision making by subjecting their expansionary activities to the scrutiny of the capital markets. If the managers of firms with substantial free cash flows have a tendency to over invest by accepting marginal investment projects with negative net present values, an increase in the dividend will, other things being equal, reduce the extent of overinvestment and raise the market value of the firm. A decrease in dividend will produce the opposite result. Therefore, “except for firms with profitable unfunded investment projects, prices will rise with unexpected increases in payouts to shareholders or promises to do so, and prices will fall with reductions in
payments or reductions in promises to make future payments” (Jensen, 1988). Consistent with this hypothesis, Lang and Litzenberger (1989) find that the average return on the announcement-day of sizable changes in dividends is significantly higher for over investing firms than for their value-maximizing counterparts, indicating that investors in the over investing firms are pleased to receive free cash flows in the form of a dividend rather than permitting them to be invested in marginal projects.

Dividend policy has been an issue of interest in financial literature since Joint Stock Companies came into existence (Frankfurter & Wood, (2002). Dividends are commonly defined as the distribution of earnings (past or present) in real assets among the shareholders of the firm in proportion to their ownership. Dividend policy connotes to the payout policy, which managers pursue in deciding the size and pattern of cash distribution to shareholders over time.

Managements’ main objective is shareholders’ wealth maximization, which interprets into maximizing the worth of the company as calculated by the price of the company’s ordinary stock. The goal can be attained by giving the shareholders a “fair” payment on their investments. Though; the impact of firm’s dividend policy on shareholders prosperity is still unresolved as examined by (Frankfurter et al, 2002). The region of corporate dividend policy has gotten attention of management scholars and economists who have conducted empirical examinations and developed theoretical models. Therefore, dividend policy is one of the major multifaceted aspects in finance. Dividend policy is of two types: managed and remaining. In remaining dividend policy the sum of dividend is just the cash left following the firms attractive investments using NPV rule .In this case the total of dividend will be extremely variable and frequently nil. If the manager believes dividend policy is significant to their investors and it absolutely influences share price assessment, they will take on managed dividend policy. The most favorable dividend policy is the one that maximizes the company’s stock price, which leads to maximization of shareholders’ wealth. Whether or not dividend decisions can add up to the value of firm is an arguable subject.

Finally, researchers partially attribute the magnitude of abnormal return generated during the dividend announcement period to the nature of dividend clientele of the firm. “[T]he dividend clientele hypothesis suggests that, ceteris paribus, the stock price response to an unexpected dividend change announcement will be related to the dividend preferences of the
marginal investor in that firm” (Denis, Denis & Sarin, (1994)). It follows that if high-yield firms attract investors in low marginal personal tax brackets and low-yield firms attract investors in high marginal tax brackets, a positive market response to a dividend increase should be more pronounced in high-yield firms than in their low-yield counterparts. Similarly, the negative response to the news of reduction in dividends should be less severe for low-yield firms than for their high-yield counterparts. The empirical evidence in support of this argument can be found in Bajaj and Vijh (1990).

2.3 Reaction of Share Market Prices to Dividend Announcements

According Manum, Hoque, Mohammad and Manum (2013) there is no gain to investors due to dividend declaration. They argued that investors’ wealth deteriorates due to shares prices declines pre and pro dividend declaration. This was attributed to continued market corrections as per regulatory requirements to minimize the chances of bullish market. In contrast listed commercial banks in Dhaka Stock Exchange between 2000 and 2013 depicted that there was no significant changes between dividend announcement and share price changes (Uddin and Uddin, 2014). In a study conducted in Ghana Stock Exchange (GSE) by Asamoah (2010) to investigate the impact of dividend announcement behavior, event study research design was applied and only three listed companies were selected. The study presumed that GSE followed the efficient market hypothesis and the stock price adjusted in relation to information availability. Non parametric statistical methods such as Wilcoxon matched pair signed rank was applied to test the null hypothesis which stipulated that the shares prices were not instantaneous to any publically declared information. The study findings depicted that GSE was not semi strong efficient and thus it must address the three forms of market efficiency. There was a significant positive relationship between stock return and dividend announcement (Bajaj & Vijh, 1990). Moreover, there was a positive significant relationship between SG-SSB share price and the dividend announcement. Similarly, Sare, Kumah and Salakpi (2014) conducted a study in GSE to examine the market’s reactions to dividend announcement. The study applied event study design whereby they studied the share price days prior to and after dividend announcement. Study findings depicted that there is a significant positive relationship between dividend announcement and shareholders returns. Moreover, there was a significant difference on the relationship between dividend announcement and specific industry sector whereby manufacturing industry had the strongest reactions to dividend announcement.
In determining the reaction of share market prices to dividend announcements the study found out that the share market is positively responsive to the dividend announcement such that the share market value of dividends improves in the few weeks after a high dividends announcement. There have been many studies that have found significant relationship between market prices and dividend announcement. Two of the studies are explained as follows. Hashemijoo, Ardekani and Younesi (2012) carried out a study to investigate the impact of dividend policy on share price volatility in the Malaysian Stock Market. The study selected a sample of 84 from 142 listed consumer companies in the main market of Bursa Malaysia. Dividend policy was measured with the use of dividend yield and pay-out. Panel data was collected for period between 2005- 2010. The study had both independent and control variables such as firm size, earning volatility, leverage, debt and growth. The study findings depicted that there is a negative significant relationship between both dividend yield and pay-out ratio with share price volatility. Amongst the control variables firm size had a negative significant relationship while earnings volatility had a positive significant relationship through the other control variables were not significant.

Duke, Ikenna and Nkamare, (2015) carried out a study in Nigerian on the impact of dividend policy on Nigerian commercial banks. The study applied correlation design to investigate the relationship. Since the data was panel in nature, several diagnostic tests such as Augmented Dickey Fuller test, unit root tests and ordinary least squares test. Results of the study depicted that there is a positive significant relationship between dividend yield and share price. Contrary to Duke, Ikenna and Nkamare, (2015) findings, there is a significant negative relationship between retained earnings and share price. According to Mukora (2014) there is a significant positive relationship between dividend announcement and shares return among the firms listed in Nairobi Securities Exchange. She established that prior to the dividend announcement the shares depicted downward trend on shares returns and an upward trend after the announcement.

Mlonzi, Kruger and Nthoesane (2011) investigated the share price reactions to earnings announcement on the JSE-Altx. The study considered all listed firms in JSE-Altx who announced their earnings within the month of January 2009. The securities price reaction was calculated using the capital asset pricing model. The study findings revealed that there was a negative share price reaction to earnings announcement among the firms listed in this stock market. Moreover, the findings depicted that the shareholders wealth was most eroded
during the recessionary period but the weak form of market efficiency provided investors with an opportunity to maximize their returns during favorable market performance.

Quoted stock prices reaction was investigated by Liyambula (2014) in Namibian stock market for years 2008 to 2011 on 12 listed firms. The study adopted an event study design. The study findings depicted that there was a positive relationship between dividend announcement and share prices reactions. It was important to note that the share price was more sensitive few days prior to announcement which was attributed to investor’s behaviour to dispose of the non-performing shares. In addition, the share prices registered a positive trend immediately after the announcement of the dividend (Liyambula, 2014).

There has been mixed empirical findings on market reactions to dividend announcement whereby some studies have reported positive and negative significant relationship between dividend announcement and reaction on share price. Therefore, Bashir, Shah and Hussain (2013) sought to investigate the reaction of share prices on dividend announcement among the firms listed in Karachi stock exchange. The study applied regression analysis to investigate the relationship of dividend announcement and share price reaction as well as firm specific factors on share prices. The study findings depicted that there was a positive significant relationship between share prices and dividend announcement. The firm’s specific factors which included size, leverage, liquidity and dividend yield registered mixed results where firm size had negative significant relationship while leverage, liquidity and dividend yield had positive significant relationship.

Adres, Betzer, Bongard, Haesner and Theissen (2009) conducted a study in Germany to investigate dividend announcement, market expectations and corporate governance. The results of the study depicted that there is a significant relationship between the market expectations and dividend announcement whereby if the dividend adhered to prior market expectation then the share prices increased after dividend announcement.

Dividend announcement is always assumed to deliver some information to investors in relation to their firms’ performance. Since the stock is always characterized as being bullish or bearish. Securities marked is said to be bullish if the stock prices are consistently on an upward trend and bearish if there are consistently on decline. There is a significant positive relationship between dividend announcement and share price on a bullish market whereas
bearish market registered a negative significant relationship. Moreover, the investors had consistent behavior if they were on the same market sector (Faloye and Oluwole, 2014).

Dharmarathne (2013) investigated the stock price reaction to dividend announcement and information in Sri Lankan share market. The study consisted of a sample of 61 major listed companies and their respective dividend announcement for the period ranging 1999 to 2005. The research design was event study. The study findings depicted that there is favorable information on dividend announcements thus there was a positive significant relationship between dividend announcement and share price. Further, the study supported the semi strong form of market efficiency whereby on average the stock prices adjusts subsequently on all publicly available information.

### 2.3.1 Linkage between Dividend Policy and Stock Price

Hashemijoo, Ardekani and Younesi (2012) carried out a study to investigate the impact of dividend policy on share price volatility in the Malaysian Stock Market. The study selected a sample of 84 from 142 listed consumer companies in the main market of Bursa Malaysia. Dividend policy was measured with the use of dividend yield and payout. Panel data was collected for period between 2005-2010. The study had both independent and control variables such as firm size, earning volatility, leverage, debt and growth. The study findings depicted that there is a negative significant relationship between both dividend yield and payout ratio with share price volatility. Amongst the control variables firm size had a negative significant relationship while earnings volatility had a positive significant relationship through the other control variables were not significant. From the study findings it was concluded that the both firm size and dividend yield had the most significant influence on share price volatility.

According to Nazir, Abdullah and Nawaz (2011) on their study on the effect of dividend policy on share price volatility among financial sector listed firms in Karachi securities exchange, they argued that firm dividend policy is most important for both investors and management since share price volatility has a significant influence on organization risk levels. In addition, to the dividend policy the study controlled the effects of earning volatility, assets growth, firm size and leverage. Multi linear regression analysis was used whereby the study applied fixed effects regression modelling. Study findings depicted that there was a significant negative relationship between dividend yield and price volatility as
well as between dividend payout and price volatility. The study concluded that dividend policy adopted by firms in the financial sector had a significant influence on share price volatility.

Salari, Abbasian, and Pakizeh (2014) investigated the relationship between the stock price volatility among non-financial listed firms in Karachi stock Exchange. The sample was based on a panel data composed of 35 quoted firms for years 2001 to 2011. The main explanatory variable was dividend yield and the controlled variables were firm size, growth, earnings per share and earning volatility. Results of the study depicted that there was a negative significant relationship between the price volatility and both dividend yield and earnings per share. In addition, there was a positive significant relationship between price volatility and firm size and growth of the asset base. Finally, there was no relationship between earnings volatility and earning volatility.

Kenyoru, Kundu and Kibiwott (2013) carried out a study to determine the impact of dividend yield on share price volatility in Kenya. The study applied panel data analysis for companies which had traded actively for the past 10 years ranging between 1998 to 2008. The study applied multiple regression analysis on the explanatory variables which were dividend payout ratio and dividend yield. The study findings depicted that the main determinants of price volatility was payout ratio which had a negative significant relationship while dividend yield had a negative significant relationship.

2.4 The Effects of Dividend Payout Ratio on Share Prices

Habib, Kiani and Khan (2012) carried out a study to examine the relationship between dividend policy and share price volatility in Pakistan stock market. The main explanatory variables were dividend yield and pay-out ratio. The study findings revealed a negative significant relationship between the pay-out ratio and share price volatility. This implies that an increase in the dividend payout ratio was associated with a decrease in the share prices.

Lashgari and Ahmadi (2014) carried out a study to investigate the impact of dividend policy on share price volatility in Tehran stock Exchange. The target population of the study consisted of 470 listed companies and a sample of 51 companies were selected through a certain stipulated inclusion criteria. The share price change was measured using Parkinson’s stock price volatility. Prior to data analysis various statistical for stationarity such as Unit
root test, Chaw test and Hausman test were carried from which pooled and fixed effects model were selected to investigate the relationship. The study findings were that there was a negative significant relationship between dividend payout ratio and price volatility while asset growth rate influenced price volatility negatively.

Oyinlola and Ajeigbe (2014) investigated the impact of dividend policy on stock prices of quoted firms in Nigeria. Secondary data was collected among listed firms for the period between 2009 and 2013. Various regressions diagnostic tests were carried out such as variance inflation test to test for heteroskedasticity as well as correlation coefficient to test for multicollinearity. Regression analysis was used to test the relationship between dividend payout and price volatility which depicted a positive significant effect on the share price.

Parsian Koloukhi and Abdolnejad (2004) argued that organization management must be concerned about the dividend payment decision. This is because the sustainability of the dividend payment affects investor’s wealth evaluation. In view of this they carried out a study to investigate the relationship between dividend payout and future company’s growth as measured by changes in the share prices. Study findings depicted a positive significant relationship between dividend payout and future company’s growth therefore a positive change in dividend payment can be associated with an increase in share prices. They concluded that through the anticipated dividend payment a firm can be in a position to evaluate its changes in value.

Salari, Abbasian and Pakizeh (2014) carried out a study to determine the impact of dividend policy on stock price volatility by considering firms listed in Tehran Stock Exchange for a period between 2001-2012. Dividend policy was measured using dividend payout ratio and dividend yield. The study findings depicted that there is a negative significant relationship between dividend payout ratio and share price volatility. Among the controlled variables which were firm size, earning volatility, debt and growth; both size and debt showed a positive significant relationship with price volatility. In addition, there was no significant relationship between share price volatility and earning volatility and growth of the firms.
2.5 Chapter Summary

The chapter takes into consideration the effects of dividend policy of share prices. The chapter commences with introduction of the topic under study whereby it introduces the studies done on the topic, dividend hypothesis and policy. Relationship between dividend policy and dividend payout ratio is explained, dividend announcement and share prices, dividend and future earnings is explained into detail. The chapter ends by exploring on the on the effect of divided payout ratio on share prices. The next chapter provides the methodology of the study where a breakdown of the data collection and analysis methods is outlined.
CHAPTER THREE
3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the methods that were used in the collection of data pertinent in answering the research question. It is divided into research design, population and sampling design, data collection methods, data analysis methods and chapter summary.

3.2 Research Design

This study adopted a descriptive research design. According to Cooper and Schindler (2003), a descriptive study relates and measures cause and effect relationship among variables. The design was deemed appropriate because the main interest was to establish the effects of dividend policy on share prices in the case study of companies listed in NSE. According to Mugenda and Mugenda (2003), the descriptive research collects data in order to answer questions concerning the current status of the subject under study and in this case, the study aimed at investigating three areas which formed our independent variables which are the considerations made before announcement of dividends, reaction to the share market prices on dividend announcements and the effects of dividend payout ratio. The dependent variables was the effects of dividend policy on share prices

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Dependent Variable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consideration before dividend announcement</td>
<td>Effects of dividend policy on share prices</td>
</tr>
<tr>
<td>Dividend payout ratio</td>
<td></td>
</tr>
</tbody>
</table>

Figure 3.1: Dependent and Independent Variables
3.3 Population and Sampling Design

3.3.1 Population
A population is defined as a complete set of individuals, cases or objects with some common observable characteristics (Mugenda and Mugenda, 2003). The study targeted all sectors of the Nairobi Securities Exchange where at the time 59 companies had been listed in the various sectors of agriculture, Commercial and service sector, finance and investment and the industrial and allied sectors.

Table 3.1 Population Distribution

<table>
<thead>
<tr>
<th>Sectors Listed in the N.S.E</th>
<th>Total Number of Companies</th>
<th>Population Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>11</td>
<td>19</td>
</tr>
<tr>
<td>Commercial and Service</td>
<td>14</td>
<td>24</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>16</td>
<td>27</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>18</td>
<td>31</td>
</tr>
<tr>
<td>Total</td>
<td>59</td>
<td>100</td>
</tr>
</tbody>
</table>

3.3.2 Sampling Design

3.3.2.1 Sampling Frame
Mugenda and Mugenda (2003) defines sampling frame as a list, directory or index of cases from which a sample can be selected. The sampling frame was sourced from the list of companies in the N.S.E. The sampling frame describes the list of all population units from which the sample will be selected (Cooper and Schindler, 2003). It is a physical representation of the target population and comprises all the units that are potential members of a sample (Kothari, 2007).

3.3.2.2 Sampling Technique
The study used stratified random sampling procedure to select a sample that represented the entire population. According to Kothari (2007), a stratified random sample is an appropriate technique used for the population that is not homogeneous. The study adopted the use of secondary data that had been obtained from N.S.E between the study periods of 2007 to 2011. This information included the stock share prices, the earnings per share and dividends paid out on the earnings of each share. The dividend payout ratio (DPOR) was then obtained from these data according to the study objectives. Comparison was made on the share prices and the dividend paid out to establish if a relationship exists in the variables.
3.3.2.3 Sample Size

According to Mugenda and Mugenda (2003), a good sample consists at least 10%-30% of the representative population. In the current study, 50% of the total population was considered as the sample, thus 30 companies were considered. According to Kothari (2007), sample size choice can also be pegged to reliability factors such as cost and efficiency especially when dealing with a large population or a long term research.

Table 3.2 Sample Size

<table>
<thead>
<tr>
<th>Sectors Listed in the N.S.E</th>
<th>Total Number of Companies</th>
<th>Sample Companies Used</th>
<th>Sample Percentage relative to the total number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>11</td>
<td>6</td>
<td>50%</td>
</tr>
<tr>
<td>Commercial and Service</td>
<td>14</td>
<td>7</td>
<td>50%</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>16</td>
<td>8</td>
<td>50%</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>18</td>
<td>9</td>
<td>50%</td>
</tr>
<tr>
<td>TOTALS</td>
<td>59</td>
<td>30</td>
<td>50%</td>
</tr>
</tbody>
</table>

3.4 Data Collection Methods

According to Ngechu, (2004) there are many methods of data collection. The choice of a tool and instrument depends mainly on the attributes of the subjects, research topic, problem question, objectives, design, expected data and results. This is because each tool and instrument collects specific data. Secondary data was collection through the use of document guide index as indicated in appendix 1V. Through the use of the guide index data was extracted from published reports of the quoted companies in the N.S.E library. In addition, NSE marked statistics for the same period was considered from which prevailing securities prices were collected.

3.5 Research Procedures

The researcher designed the data tool to reflect the various parameters that would best represent the research questions. Thereafter, the questionnaire was discussed with lecturers and fellow class mates. According to Kothari (2007) through pilot study a researcher is in a position to identify the faults in the research instrument and make correction prior to the actual study. Piloting was carried out in eight companies two from each market sector. These
companies were excluded in the final study sample size. Through pretesting the researcher ascertained the validity and reliability of the study instrument.

3.6 Data Analysis Methods

The researcher perused completed documents on market share prices document guide index recording sheets. The information was displayed by use of line graphs and in prose-form. This was done by tallying up responses, describing and interpreting the data in line with the study objectives and assumptions through use of SPSS. Regression analysis was carried out for the second and third objective of the study to determine the nature of the relationship between the dependent variable (share price) and the independent variable (announcement of the dividend and the dividend payout ratio). Correlation analysis was used to describe the degree to which one variable is related to the other. The relationship, if any, is usually assumed to be linear. In this study coefficient of correlation (r) and coefficient of determination (r²) was estimated to determine the nature and magnitude of the relationship. Correlation coefficient was used to measure the degree or magnitude of relationship between dividend payout and the firm’s share market prices. The magnitude of the sample coefficient of correlation indicates a weak or strong linear relationship.

3.7 Chapter Summary

The chapter has set out the methodology to be used in the study. The study comprised of firms at the NSE; the chapter outlines that secondary data was used in the study. The data was obtained from the NSE statistics. Data was analyzed by use of simple linear regression and correlation analysis and coefficient of determination was used to establish how well the regression line fits the data. Chapter four therefore uses the data that was been obtained from the listed companies and analyses them to establish if a relationship exists in the dividends being paid out by companies to the share prices from these companies.
CHAPTER FOUR
4.0 RESULTS AND FINDINGS

4.1 Introduction

This chapter presents a summary of the findings on effect of dividend policy on share prices of the firms listed at the N.S.E for the period 2007 to 2011. These findings are presented in this chapter in both graphical and prose-form to enhance great usability. For the period 2007 to 2011, the results indicated that there is a relationship between dividend payout and share price.

4.2 General Characteristics of Some of the companies analysed

In the current section a comparative analysis is carried out amongst the different companies under consideration. A case of Rea Vipingo depicted that there was an upward trend when the payout ratio was more than zero percent and a down ward trend if the dividend payout ratio was zero. For example in the year 2009 the payout ratio was 60.98% and the market price per share increased from Sh 2.70 to Sh 5. Similarly, in the year 2010 the payout ratio was 37% and the market price per share rose to 20.75 from Sh 16.90 in the previous year.

An analysis of Kakuzi stock price in relation to the amount of payout ratio, in the year 2008 the payout ratio was nil and the stock price was Sh 28, the price declined to Sh 19.50 after the company paid out nil dividends in 2009. An upward price trend was observed in 2010 to Sh 45.50 after the payout ratio increased to 23.41%. In the year 2011 the stock price declined to Sh 41.70 after the payout ratio decline to 21.6%. In contrast in year 2012 the stock price increased to Sh 45 after the payout ratio increase to 25.12%.

An analysis of Sasini tea depicted that in 2008 the share price was Sh 15 and the payout ratio was 34.36%. After an increase of payout ratio to 61.73% the share price rose to Sh 21. There was a decline in stock price from Sh 21 to Sh 20.50 after the dividend payout ratio declined to zero in year 2010. Despite the payment of 16.06% as dividend in the year 2011 the stock price remained stagnant at Sh 20.50.

In 2008 Williamson tea had a payout ratio of 12.72% while the market price was Sh 41.25. In 2009 the payout ratio rose to 70.89% while the market price increased to Sh 84. Despite
of the changes in the dividend payout ratio the share price maintained an upward trend in year 2009 to 2010 with the highest price being Sh 143. There was a sharp decline in market price to Sh 40.25 after the dividend payout decline to 7.95%.

In year 2007, Kenya Airways had a payout ratio of 31.91% and a market price per share of Sh 7.25. Although, the dividend payout ratio increased to 66.67% in year 2008 the market price per share declined to Sh 6.50. Similarly, in year 2009 the dividend payout ratio declined to 26.59% while the market price per share increased to Sh 11.85. A similar trend was noted in year 2010 when the market price increased to Sh. 34.50 and the dividend payout decreased to 19.11%. In year 2011, there was a decline in market share to Sh 32.80 the dividend payout ratio also declined to 16.73%.

An analysis of market share price sensitivity to the dividend payout policy depicts that in year 2008 Nation media dividend payout was 32.78% and the security price was Sh. 40. After an increase in the dividend payout ratio to 33.11% the share price increased to Sh 101. In the year 2010 the dividend payout ratio increased to 50.03% and the share price increased to Sh. 195. After increasing the dividend payout ratio to 59.74% in year 2011 the stock price increased to Sh. 201.

In the year 2007, TPS Serena had a dividend payout ratio of 51.16% and the market price was Sh. 16. After increasing the payout ratio to 51.16% the share price increased to Sh. 20 in the year 2008. There was a sharp price increment in year 2009 to Sh 81.00 after an increase in dividend payout ratio to 135.42%.

In the year 2008 when Barclays bank had a dividend payout ratio of 89.06% the share price was Sh. 85. The share price rose to Sh. 131 despite the dividend payout ratio decline to 77.21% in 2009. An upward trend was noted in the year 2010 to Sh. 204 which remained stagnant even in the year 2011.

An analysis of the Diamond Trust bank share price in relation to the company’s payout policy revealed that in year 2008 the payout ratio was 78.43% and the share price was Sh 9. Despite a decline in the payout ratio in year 2009 to 63.16% the market price per share increased to Sh. 21.50. A similar trend was noted in year 2010 when the payout ratio
declined to 42.42% and the market price per share increased to Sh. 32.25. Even though the reduction of the payout ratio to 28.65% in year 2011 the share price remained stagnant at Sh 44.75.

In the year 2008 Total Kenya dividend payout ratio was zero and the market price was Sh 10.35. In the year 2009 the share price rose to Sh. 35.75 after the dividend payout ratio increased to 70.54%. The share price registered an upward trend to Sh 41 in year 2010 after an increase in the dividend payout ratio to 81.37%. Despite an increase in dividend payout ratio to 88.98% in year 2011 the share price decreased to Sh. 34.75.

In the banking sector NIC bank had a dividend payout ratio of 47.49% in 2007 and its market price was Sh. 15.25. Despite an increase of payout ratio to 52.63% the market price declined to Sh 13.10 in year 2008. In the year 2009 the payout ratio increased to 71.94% while the share price increased to Sh 26. The share price increased to Sh 52.50 in year 2010 after an increase in payout ratio to 75.68%. After a decrease in the payout ratio to 74.75% the share price decreased to Sh 52.

In the year 2007 KCB dividend payout ratio was zero and the share price was Sh 19.10. There was a sharp decline in share price in 2008 to Sh 10.15 after the company paid nil dividends. Despite the persistent zero dividend payout ratios in year 2009 the share price increased to Sh 47.25. In year 2010 the payout ratio increased to 50.72% and the share price increased to Sh 66.5 and in year 2011 the payout ratio was 60.21% and the share price rose to Sh 115.

In the year 2007 KCB had a payout ratio of 68.59% and the share price was Sh 54. After an increase in payout ratio to 173.4% the share price declined to Sh 47.50. The share price increased to Sh 98 after the dividend payout decrease to 85.05%. In contrast in year 2010 the share price increased to Sh 245 after the payout increased to 136.34%. Despite the reduction of the dividend payout ratio to 90.45% in year 2011 the share price increased to Sh. 200.

In 2007 the dividend payout ratio for EABL was 68.44% while the share price was Sh 80. After the reduction of the payout ratio in 2008 to 60.48% the share price increased to Sh 82.50. There was an increase in the share price in 2009 to Sh 226 after an increase in payout
ratio to 87.85%. Despite a decrease in payout ratio to 51.36% in 2011 the share price increased to Sh 445. In 2011 the payout ratio increased to 62.17% and the share price decreased to Sh 149.

In 2007 Bamburi had a dividend payout ratio of 57.8% while the share price was Sh 29.00. After the reduction of the payout ratio to 37.31% the price per share reduced to Sh 17.25. After an increase in the dividend payout ratio to 29.59% the market price per share increased to Sh 80. Although, the payout ratio was 129.3% in 2010 the share price remained stagnant at Sh 80, the price increased in 2011 to Sh 140 after a decrease in the payout ratio to 89.27%.

In 2007 BOC Company had a payout ratio of 92.69% and the share price was Ksh31.00. In 2008 the dividend payout ratio decreased to 92.45% while the share price reduced to Sh 27. Although in 2009 the payout ratio decreased to 80.56% the share price increased to Sh 75.50. Despite reduced payout ratio in 2010 to 54.87% the share price increased to Sh 116, while in 2011 the price increased to Sh 117 and the payout ratio increased to 59%.

4.3 Considerations Made Before the Announcement of the Dividends

The study found by way of foot notes on the financial statements indicated that the listed companies in N.S.E considered the following actors before issuing shares in any previous period, the dividends to be given to the preferred shareholder, what the rival companies pay, the net earnings during the period, the amount in the reserves and the investment prospects before issuing shares in any period. The Dividend policy remains a basis of controversy in spite of years of theoretical and empirical research, including one characteristic of dividend policy namely: the connection between dividend policy and stock price. They may also influence the perceptions of the investors about the briskness of the company by following a stable dividend policy where the actual briskness of the company remains unchanged. This sort of argument is known as the dividend signaling hypothesis. Nevertheless, there is an abundance of evidence associating announcements of changes in dividends with abnormal share price performance.

The findings obtained from the N.S.E market analysis indicated that the announcement of increases in dividends are associated with significant positive abnormal/excess returns and the announcement of decreases in dividends are associated with significant negative
abnormal/excess returns while the announcement of no-changes in dividends produce only normal returns for shareholders. This market phenomenon is known as the dividend announcement effect, meaning an increase in the dividend will, other things being equal, reduce the extent of over-investment and raise the market value of the firm. A decrease in dividend will produce the opposite result. It was found that partially attributed the magnitude of abnormal return generated during the dividend announcement period to the nature of dividend clientele of the firm. Similarly, the negative response to the news of reduction in dividends should be less severe for low-yield firms than for their high-yield counterparts.

The statistics established that in an imperfect market the firm should consider the possible effects of the differential tax brackets of its shareholders, dilution of control, flotation and transaction costs the stability of earning etc, when reaching its dividend decision. It is equally clear that in an imperfect market the firm should consider the possible effects of the differential tax brackets of its shareholders, dilution of control, flotation and transaction costs the stability of earning etc, when reaching its dividend decision. This was due to the fact that it was not clear if dividends would be preferred to capital gains or vice versa.

The apparent collective market judgment about the desirability of dividends does not take into account the opportunities for profitable reinvestment of such fund. The Investors may have superior self-assurance that reported earnings reflect fiscal profits when announcements are accompanied by abundant dividends. If investors are more convinced in their opinions, they may respond less to dubious sources of information and their anticipation of value may be insulated from illogical influence. Although expanding firms may have lower payout ratio and dividend yield, there share prices show consistency. This perhaps may be because dividend yields and payout ratio serves as proxies for the quantity of predictable growth opportunities.

The forecasts of profits from growth opportunities are less dependable than forecasts of returns on possessions in place, firms with low payout and low dividend yield may have better price stability. On duration result and arbitrage effect, the dividend yield and not the payout ratio is the relevant gauge. Rate of return outcome entails that both dividend yield and payout ratio matters. Dividend policy may serve as a proxy for development and investment opportunities. In cooperation, the duration consequence and the rate of return
effect suppose differentials in the timing of the primary cash flow of the business. If relationship between risk and dividend policy relics after controlling for growth, it would propose proof of either the arbitrage or information effect. Residual dividend policy dividend payout ratio is where dividends are paid out of earnings left over after investment decisions have been financed.

The findings from the secondary data used indicated that dividends were only paid if there are no profitable investment opportunities available. The policy is consistent with shareholders wealth maximization. Higher payout ratios do not lead to higher, real dividend growth. The dividend policy and a payout ratio, consequently, can make major impact on the company future value when well established and cautiously followed. Corporate governance institutes an effective mechanism of how much to pay as share dividends and when to pay, taking into account a variety of factors relating to the company's current status, its future as well as market and economic circumstances. If forecasts of proceeds from growth opportunities are less dependable than forecasts of returns on assets available, firms with low dividend yield and low payout may have greater price volatility.

Dividend policy may serve as a proxy for growth and investment opportunities. Together, the duration effect and the rate of return effect suppose a degree of difference in the timing of the primary cash flow of the business. If the relationship between risk and dividend policy remains after controlling for growth, it would recommend facts of either the arbitrage or information effect.

**4.4 Reaction of Share Market Prices to dividend announcements**

Figure 4.1 shows trend analysis for the entire market for the period under study. Analysis for the entire market presented in the line graph above shows that generally, as the DPOR rises, the share prices for the entire market rises while they both fall concurrently. This clearly shows a direct relationship between DPOR and market share prices.
Figure 4.1: Share Price against Time for the Entire Market

Table 4.1 below shows the model summary for the regression analysis between the market price and the announcement of the DPOR ratio in the entire market. The R squared was 0.54 which shows the model explanatory power depicted that 54% of the changes in the share price in the entire market can be explained by the announcement of DPOR while the remaining percentage can be explained by other factors excluded in the model. The adjusted R square was 53.4% which shows the model explanatory power with the exclusion of the constant variable in the regression model. In addition, the coefficient for R was 0.735 which shows the correlation coefficient between the market price and the announcement of DPOR, since the coefficient was 0.735 it depicts that there is a strong positive relationship between DPOR and the share price thus in the entire market as the DPOR increases the share also increases and vice versa. In all the regression models in this chapter the standard error of estimates shows the average deviation from the linear of best among the variables under investigation.

Table 4.1: Entire Market Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.735a</td>
<td>0.540</td>
<td>0.534</td>
<td>0.459</td>
</tr>
</tbody>
</table>

a Predictors: (Constant). DPOR.
ANOVA (Analysis of Variance)

The F statistics is used as a test for the model goodness of fit, \((F=37.210, \ p \ value <0.05)\) shows that there is a significant relationship between market price per share and the announcement of DPOR in the entire market and at least the slope (\(\beta\) coefficient) is not zero. The regression sum of squares shows the sum of the squared deviation from the line of best fit to the respective observed variables, residual sum of squares shows the sum of squared deviations which cannot be explained by the model while the total sum of squares shows the sum of squared deviations which has been explained and unexplained by the regression model. The degrees of freedom for the regression model was 1 corresponding with the number of independent variables (announcement of DPOR) and 148 in overall corresponding with the response rate minus 1 while the degrees of freedom for residual were 148 (149-1). The F statistics is the ratio between regression mean sum of square and residual sum of squares.

Table 4.2: ANOVA for the Entire Market

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>35.423</td>
<td>1</td>
<td>35.423</td>
<td>37.210</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>140.892</td>
<td>148</td>
<td>0.952</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>176.315</td>
<td>149</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The regression coefficients were used to show the nature of the relationship between the announcement DPOR and the share price in the entire market. The study findings revealed that there was a positive significant relationship between the announcement of DPOR and the share price in the entire market since the t ratio was 4.9 and the p value was less than 0.05 \((\beta=0.686, \ t= 4.900, \ P \ value < 0.05)\). This implies that a unit increase in the DPOR leads to 0.686 increase in share price in the entire market.
Table 4.3 Regression Coefficient for the Entire Market

<table>
<thead>
<tr>
<th>Variables</th>
<th>B</th>
<th>Std. Error</th>
<th>Beta</th>
<th>t</th>
<th>P value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>0.878</td>
<td>0.212</td>
<td></td>
<td>4.142</td>
<td>0.000</td>
</tr>
<tr>
<td>DPOR</td>
<td>0.686</td>
<td>0.14</td>
<td>0.735</td>
<td>4.900</td>
<td>0.000</td>
</tr>
</tbody>
</table>

4.5 Dividend Payout Policy and Share Prices

The research utilizes the information on a number of companies that are listed in the NSE under various sectors depending on the specialty of the company; the agricultural sector involves companies that grow, sell and market the agricultural products within and outside the country. The commercial and service sector constitutes of companies that invests in the major commercial sectors of the country and those that provides the necessary services which keeps the economy growing and moving forward, and these services are on the major sectors of the economy such as transportation, communication and media.

Finance and investment sector are the financial institutions that operates on the sectors of banking and the financing on the various projects to individuals and groups. The industrial and allied sector makes it the pillars of the economy as they invest mainly on the resources available and produce finished products that can either be used within the country or they may be exported outside the country. The research therefore analyzes each sector of the NSE and uses data from the companies that were selected for study to try and obtain if a relationship exists in the share prices and the dividend paid out at different time periods.

4.5.1 Agricultural Sector Market Analysis

The trend analysis for the agricultural sector of the NSE as regards dividend pay-out ratios and share prices is shown in Figure 4.2 below. The pictorial presentation depicts that initially the agricultural sector was characterised by an upward trend in the share prices followed by downward trend and finally an upward trend. Similarly, the dividend payout ratio was characterised by stagnation, then upward trend before declining slowly as the share price increased in the later years.
Figure 4.2: Share Price against Time in years for the Agricultural Sector

Table 4.4 shows the regression model summary for the relationship between the DPOR and the share price in the agricultural sector. The correlation coefficient depicts that there is a strong positive relationship between DPOR and market share price in the agricultural sector as depicted by R of 0.645. In addition, the findings revealed that 41.6% of the changes in the share price can be explained by the DPOR in the agricultural sector.

Table 4.4: Regression Model Summary for Agricultural Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.645a</td>
<td>0.416</td>
<td>0.397</td>
<td>0.0423</td>
</tr>
</tbody>
</table>

a Predictors: (Constant), DPOR.

ANOVA (Analysis of Variance)

The F statistics is used as a test for the model goodness of fit, (F=35.46, p value <0.05) shows that there is a significant relationship between market price per share and the DPOR in the agricultural sector and at least the slope (β coefficient) is not zero.
Table 4.5: ANOVA for the Agricultural

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>45.153</td>
<td>1</td>
<td>45.153</td>
<td>35.46</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>35.644</td>
<td>28</td>
<td>1.273</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>80.797</td>
<td>29</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The regression coefficients were used to show the nature of the relationship between the DPOR and the share price in the agricultural sector. The study findings revealed that there was a positive significant relationship between the DPOR and the share price in the agricultural sector since the t ratio was 3.057 and the p value was less than 0.05 ($\beta=0.749$, $t=3.057$, $P$ value < 0.05). This implies that a unit increase in the DPOR leads to 0.749 increase in share price in the agricultural sector.

Table 4.6: Regression Coefficient for the Agricultural Sector

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>P value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>0.549</td>
<td>0.188</td>
<td>2.913</td>
<td>0.000</td>
</tr>
<tr>
<td>DPOR</td>
<td>0.749</td>
<td>0.245</td>
<td>0.645</td>
<td>3.057</td>
</tr>
</tbody>
</table>

4.5.2 Commercial and Services Sector

The trend analysis for the commercial and service sector of the NSE in regard to dividend pay-out ratios and share prices is shown in Figure 4.3 below. The pictorial presentation depicts that the commercial and services sector was characterised by an upward trend in both the market price and the DPOR and in year 2010 the sector had a pick in both share price and DPOR then it both exercised a down ward trend.
Figure 4.3: Share Price against Time for the Commercial Services Sector

Table 4.7 shows the regression model summary for the relationship between the DPOR and the share price in the commercial and service sector. The correlation coefficient depicts that there is a strong positive relationship between DPOR and market share price in the commercial and services sector as depicted by R of 0.845. In addition, the findings revealed that 71.4% of the changes in the share price can be explained by the DPOR in the commercial and services sector.

Table 4.7: Regression Model Summary for Commercial and Services Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.845a</td>
<td>0.714</td>
<td>0.697</td>
<td>0.0513</td>
</tr>
</tbody>
</table>

a Predictors: (Constant). DPOR.

ANOVA (Analysis of Variance)

The F statistics is used as a test for the model goodness of fit, (F=39.451, p value <0.05) shows that there is a significant relationship between market price per share and the DPOR in the commercial and services sector and at least the slope (β coefficient) is not zero.

Table 4.8: ANOVA for the Commercial and Services Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>d.f</th>
<th>Mean Squar</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>56.145</td>
<td>1</td>
<td>56.145</td>
<td>39.451</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>46.959</td>
<td>33</td>
<td>1.423</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>103.104</td>
<td>34</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The regression coefficients were used to show the nature of the relationship between the DPOR and the share price in the commercial and services sector. The study findings revealed that there was a positive significant relationship between the DPOR and the share price in the commercial and service sector since the t ratio was 3.057 and the p value was less than 0.05 (β=0.785, t= 5.377, P value < 0.05). This implies that a unit increase in the DPOR leads to 0.785 increase in share price in the commercial and service sector.
Table 4.9: Regression Coefficient for Commercial and Services Sector

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>P value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>0.342</td>
<td>0.112</td>
<td></td>
<td>3.054</td>
</tr>
<tr>
<td>DPOR</td>
<td>0.785</td>
<td>0.146</td>
<td>0.845</td>
<td>5.377</td>
</tr>
</tbody>
</table>

4.5.3 Finance and Investment Sector

A trend analysis for the relationship between dividend payout policy and share prices is shown in Figure 4.4 below. The market price per share experienced an upward trend through the period under consideration with the steepest increase being between 2008 and 2009. The dividend payout ratio had mixed trends of up and down during the period under consideration. It was interesting to note that in the year 2008 to 2009 the share price had the steepest trend while the DPOR had a downward trend.

![Figure 4.4: Share Price against Time for the Finance and Investment Sector](image)

Table 4.10 shows the regression model summary for the relationship between the DPOR and the share price in the finance and investment sector. The correlation coefficient depicts that there is a strong positive relationship between DPOR and market share price in the finance and investment sector as depicted by R of 0.549. In addition, the findings revealed that 30.14% of the changes in the share price can be explained by the DPOR in the finance and investment sector.
Table 4.10: Regression Model Summary for Finance and Investment Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.549a</td>
<td>0.3014</td>
<td>0.284</td>
<td>0.0142</td>
</tr>
</tbody>
</table>

a Predictors: (Constant), DPOR,

ANOVA (Analysis of Variance)

The F statistics is used as a test for the model goodness of fit, (F=28.56, p value <0.05) shows that there is a significant relationship between market price per share and the DPOR in the finance and investment sector and at least the slope (β coefficient) is not zero.

Table 4.11: ANOVA for the Finance and Investment Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>d.f</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>45.123</td>
<td>1</td>
<td>45.123</td>
<td>28.56</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>68.40</td>
<td>38</td>
<td>1.80</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>113.523</td>
<td>39</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The regression coefficients were used to show the nature of the relationship between the DPOR and the share price in the finance and investment sector. The study findings revealed that there was a positive significant relationship between the DPOR and the share price in the finance and investment sector since the t ratio was 6.781 and the p value was less than 0.05 (β=0.712, t= 6.781, P value < 0.05). This implies that a unit increase in the DPOR leads to 0.712 increase in share price in finance and investment sector.
### Table 4.12: Regression Coefficient for the Finance and Investment Sector

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>P value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>0.312</td>
<td>0.101</td>
<td>3.12</td>
<td>0.000</td>
</tr>
<tr>
<td>DPOR</td>
<td>0.712</td>
<td>0.105</td>
<td>6.781</td>
<td>0.000</td>
</tr>
</tbody>
</table>

#### 4.5.4 Industrial & Allied sector

For the industrial and allied sector, as the DPOR rose in 2007, the share prices fell slightly during the same year and as the market share prices rose sharply in 2008 and 2009 the DPOR fell and rose in the same period and both fell in 2010 with the fall in share prices being sharper. It can be concluded therefore there is some slight relationship between DPOR and the market share prices in the industrial and allied sector.

![Figure 4.5: Trend Analysis for the Industrial and Allied Sector](image)

Table 4.13 shows the regression model summary for the relationship between the DPOR and the share price in the industrial and allied sector. The correlation coefficient depicts that there is a strong positive relationship between DPOR and market share price in the finance and investment sector as depicted by R of 0.652. In addition, the findings revealed that 42.5% of the changes in the share price can be explained by the DPOR in industrial and allied sector.
Table 4.13: Regression Model Summary for Industrial and Allied Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.652a</td>
<td>0.425</td>
<td>0.402</td>
<td>0.058</td>
</tr>
</tbody>
</table>

a Predictors: (Constant), DPOR,

ANOVA (Analysis of Variance)

Model goodness of fit was tested using F statistics, (F=15.426, p value <0.05) shows that there is a significant relationship between market price per share and the DPOR in the industrial and allied sector and at least the slope (β coefficient) is not zero.

Table 4.14: ANOVA for the Industrial and Allied Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>d.f</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>28.546</td>
<td>1</td>
<td>28.546</td>
<td>15.426</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>23.2329</td>
<td>43</td>
<td>0.5403</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>51.7789</td>
<td>44</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The regression coefficients were used to show the nature of the relationship between the DPOR and the share price in the industrial and allied sector. The study findings revealed that there was a positive significant relationship between the DPOR and the share price in the industrial and allied sector since the t ratio was 2.561 and the p value was less than 0.05 (β=0.548, t= 2.561, P value < 0.05). This implies that a unit increase in the DPOR leads to 0.548 increase in share price in industrial and allied sector.

Table 4.15: Regression Coefficient for the Industrial and Allied Sector

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>P value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>0.879</td>
<td>0.156</td>
<td>5.635</td>
<td>0.000</td>
</tr>
<tr>
<td>DPOR</td>
<td>0.548</td>
<td>0.214</td>
<td>0.652</td>
<td>2.561</td>
</tr>
</tbody>
</table>
4.5.5 Regression Analysis for the Entire Market

Table 4.16 shows the regression model summary for the relationship between the DPOR and the share price in the finance and investment sector. The correlation coefficient depicts that there is a strong positive relationship between DPOR and market share price in the finance and investment sector as depicted by R of 0.746. In addition, the findings revealed that 55.7% of the changes in the share price can be explained by the DPOR in the entire market.

Table 4.16: Regression Model Summary for the Entire Market

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.746a</td>
<td>0.557</td>
<td>0.540</td>
<td>0.042</td>
</tr>
</tbody>
</table>

a Predictors: (Constant). DPOR.

ANOVA (Analysis of Variance)

In Table 4.17 the F statistics is used as a test for the model goodness of fit, (F=26.452, p value <0.05) shows that there is a significant relationship between market price per share and the DPOR in the entire market and at least the slope (β coefficient) is not zero.

Table 4.17: ANOVA for the Entire Market

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>d.f</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>42.451</td>
<td>1</td>
<td>42.451</td>
<td>26.452</td>
<td>.000</td>
</tr>
<tr>
<td>Residual</td>
<td>237.5104</td>
<td>148</td>
<td>1.6048</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>279.9614</td>
<td>149</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

In Table 4.12 the regression coefficients were used to show the nature of the relationship between the DPOR and the share price in the entire market. The study findings revealed that there was a positive significant relationship between the DPOR and the share price in the entire market since the t ratio was 3.296 and the p value was less than 0.05 (β=0.412, t=3.296, P value < 0.05). This implies that a unit increase in the DPOR leads to 0.412 increase in share price in the entire market.
Table 4.12: Regression Coefficient for the Industrial and Allied Sector

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>P value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>0.985</td>
<td>0.216</td>
<td>4.56</td>
<td>0.000</td>
</tr>
<tr>
<td>DPOR</td>
<td>0.412</td>
<td>0.125</td>
<td>0.746</td>
<td>3.296</td>
</tr>
</tbody>
</table>

4.6 Chapter Summary

The current chapter has presented both the study findings and interpretations. The findings are organized as per the study objectives. The study findings depicted that share prices have a positive significant relationship with the announcement of the company’s dividend payout ratio. Therefore, when a firm declares positive news or negative news to the public the information is quickly adjusted on the share prices. The findings are in tandem with the efficient market hypothesis theory which postulates that whenever positive news are declared publicly then the share price must increase and vice versa. Moreover, the findings revealed that there is a positive significant relationship between the share prices and the dividend payout ratio as practiced in the four sectors of the NSE market at the time of the study. Further, all the sectors depicted that there is a strong positive relationship between the DPOR and the share prices among the companies quoted in NSE in all the four sectors the findings were in agreement with the signaling hypothesis which postulates that whenever a firm pays dividend then the firm had registered some positive performance in the previous year and the investors postulates that similar trend will be repeated in the future. The next chapter presents the summary, discussion, conclusion and recommendations from the study.
CHAPTER FIVE

5.0 DISCUSSION, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The current chapter presents the summary of the data findings on the current status of the effects of dividend policies on the share prices among the firms quoted in NSE. The chapter is structured into the summary of the findings, discussion of the findings, conclusion, recommendation and suggestion for further studies.

5.2 Summary

The general objective of the study was to establish the effect of dividend policy on the value of the share price. The specific objectives of the study were to investigate the considerations made before announcement of dividends, to investigate the reaction of share market prices to dividend announcements, and to examine the effects that dividend payout ratio has on share prices. The study adopted a descriptive research design to establish the effects of dividend policy on share prices. The research adopted secondary data from the information that had been listed regarding the performance of the companies between the given time periods when the study was being carried out. The data obtained had information on the share prices and dividend paid out on the earning of each share after a certain period that the company had been in operation. This information was then compiled on the different companies in different sectors to establish if a relationship existed in the share prices and dividend that was being paid out from the earnings of the shares. The information was displayed by use of line graphs, tables and in prose-form. This was done by tallying up responses, describing and interpreting the data in line with the study objectives and assumptions through use of SPSS. Regression analysis was carried out to determine the nature of the relationship between the market share price and the DPOR.

The results of the study revealed that there are several considerations which are made prior to issuing dividends to the shareholders. These include: dividends paid in the previous period, the dividends to be given to the preferred shareholder, what the rival companies pay, the net earnings during the period, the amount in the reserves and the investment prospects.
The study findings depicted that there is a significant positive relationship between the dividend announcement and the share price whereby the share prices depicted an upward trajectory whenever positive dividend announcement were declared public. The study findings are consistent with the past studies which had indicated that there is a significant relationship between positive dividends announcement and share prices and the efficient market hypothesis theory.

On average, there was a significant relationship between the dividend payout ratio (DPOR) and the firm’s share price. In this regard, dividend policy is relevant to the value of share price of a listed company. From the regression and trend analysis results of the entire market it was observed that there was a positive relationship between DPOR and the market share prices though the relationship. The coefficient of correlation for the entire market was estimated to be 0.746 indicating that there is a positive relationship. The coefficient of determination for the entire market was estimated to be 0.557, which means that 55.7% of the changes in the share price were explained by the change in DPOR.

5.3 Discussion

5.3.1 Considerations made before Announcement of Dividend

The study found that companies consider dividends paid in the previous period, the dividends to be given to the preferred shareholder, what the rival companies pay, the net earnings during the period, the amount in the reserves and the investment prospects before issuing dividends. This study concurs with Benartzi et al. (2007) who investigated the market reaction to cash dividend announcements for the period 2000-2004 employing data from the Athens Stock Exchange (ASE). In particular, the paper examined both the stock price and trading volume response to dividend distribution announcements. The dividend distribution in Greece features remarkable differences from those of the US, the UK and other developed markets. First, dividends in Greece are paid annually rather than quarterly or semi-annually. Second, the Greek corporate laws designate accurately the minimum amount for distribution from the taxed corporate profits. Third, neither tax on dividends nor on capital gains is imposed. Fourth, the Greek listed firms are characterized by high ownership concentration where major owners are usually involved in management and have, therefore, less need for dividend announcements as information source. Despite this neutralized information and tax environment, the study documented significant market reaction on dividend change
announcements, lending support for the “information content of dividends hypothesis”. Relevance of dividend policy to the corporate value is owing to the market defect.

Shareholders are able to receive the return on their investment in the form of dividends or in the form of capital gains. Dividends comprise an almost direct cash payment with no selling of shares. Contrary, capital gains or losses are defined as the dissimilarity between the sell and buy price of shares. Resistance costs are one of the market defects and are additionally distinguished in transaction costs, floatation costs and taxes. Another market defect is that of information asymmetries between the insiders (like managers) and the outsiders (the investors). Agency conflicts, stemming from the diverse aim of company's stakeholders, form the third market defect. Lastly, there are other issues connected to dividend policy and cannot be located among the previously stated imperfections. This findings also concurs with a study done by Miller and Modigliani (1958) even though they proposed that no relationship should exist between the dividend policy and the market value of the firm; they admitted that “where a firm has adopted a policy of dividend stabilization with a long-established and generally appreciated target payout ratio, investors are likely to (and hence have good reason to) interpret a change in the dividend rate as a change in the management's view of the future profit prospects of the firm” (Miller and Modigliani, 1958). In this context, dividend increases (decreases) convey favorable (unfavorable) information about current and future profitability of firms to the outside investment community.

The study also agrees with Modigliani (1958) findings that under certain simplifying suppositions, a firms’ dividend policy does not influence its worth. The essential principle of their argument is that firm value is sturdily inclined to choosing most favorable investments. The net payout is the disparity flanked by earnings and investments, and a residual dividend policy dividend payout ratio. Since the net payout encompass dividends and share repurchases, a firm can regulate its dividends to any height with a counter-balance change in share exceptional of profit realized. From the viewpoint of investors, dividends policy is immaterial, as any desired stream of payments can be simulated by suitable purchases and sales of equity. As stated by Aivazian and Booth, 2003, investors will not pay a premium for any scrupulous dividend policy.

The findings of this study also agrees with Frankfurter and Wood, (2002) who noted dividends are commonly defined as the distribution of earnings (past or present)in real assets
among the shareholders in proportion to their ownership. Dividend policy has been an issue of interest in financial literature since Joint Stock Companies came into existence in 1856. Dividend policy connotes to the payout policy, which managers pursue in deciding the size and pattern of cash distribution to shareholders over time.

On the relationship between dividend announcement and share prices, the study established a positive significant relationship. These findings agree with (Faloye and Oluwole, 2014) who noted that there is a significant positive relationship between dividend announcement and share price on a bullish market whereas bearish market registered a negative significant relationship. Moreover, the investors had consistent behavior if there were on the same market sector.

5.3.2 Reaction of Share Market Prices to Dividend Announcements

In determining the reaction of share market prices to dividend announcements the study found out that the share market is positively responsive to the dividend announcement such that the share market value of dividends improves in the few weeks after a high dividends announcement. There have been many studies that have found significant relationship between market prices and dividend announcement. Two of the studies are explained as follows. Hashemijoo, Ardekani and Younesi (2012) carried out a study to investigate the impact of dividend policy on share price volatility in the Malaysian Stock Market. The study selected a sample of 84 from 142 listed consumer companies in the main market of Bursa Malaysia. Dividend policy was measured with the use of dividend yield and pay-out. Panel data was collected for period between 2005-2010. The study had both independent and control variables such as firm size, earning volatility, leverage, debt and growth. The study findings depicted that there is a negative significant relationship between both dividend yield and pay-out ratio with share price volatility. Amongst the control variables firm size had a negative significant relationship while earnings volatility had a positive significant relationship through the other control variables were not significant. From the study findings it was concluded that both firm size and dividend yield had the most significant influence on share price volatility.

The study also confirms Nazir. et al. (2011) findings on their study on the effect of dividend on policy on share price volatility among financial sector listed firms in Karachi securities exchange, they argued that firm dividend policy is most important for both investors and
management since share price volatility have a significance influence on organization risk levels. In addition, to the dividend policy the study controlled the effects of earning volatility, assets growth, firm size and leverage. Multi linear regression analysis was used whereby the study applied fixed effects regression modelling. Study findings depicted that there was a significant negative relationship between dividend yield and price volatility as well as between dividend pay-out and price volatility. The study concluded that dividend policy adopted by firms in the financial sector had a significant influence on share price volatility.

The study also agrees with a study carried out by Kenyoru. *et.al.* (2013) to determine the impact of dividend yield on share price volatility in Kenya. The study applied panel data analysis for companies which had traded actively for the past 10 years ranging between 1998 and 2008. The study applied multiple regression analysis on the explanatory variables which were dividend pay-out ratio and dividend yield. The study findings depicted that the main determinants of price volatility was pay-out ratio which had a negative significant relationship while dividend yield had a negative significant relationship.

Powell, (2000) states that even though earnings are the prime economic force behind the value of a share of equity, the actual distribution equity and such earnings has been looked upon by many analysts as an almost separate contribution to value. Other analysts and scholars have argued that increased dividends are interpreted by the market as an announcement of a permanent or expected increase in earnings. In a knowledgeable market, all involved participants hold similar information about a firm, as well as bankers, mangers, shareholders, and others. If one group has better information about the firm’s present circumstances and potential prospects, an informational asymmetry is available. The majority of academics and financial practitioners consider that managers have better information concerning their firms relative to other involved parties. Dividend alters dividend initiations and removal of dividend payments are announced frequently in the financial media. In reply to such declaration, share prices increase following dividend increases and dividend initiations, share prices frequently decline following dividend cuts and dividend eliminations. On the idea that dividend payouts can indicate a firm’s prospects appears to be well conventional amongst the chief financial officers (CFOs) of large US corporations.
The study established that dividends remained behind earnings, namely increases in earnings are followed by increases in dividends and decreases in earnings sometimes by dividend cuts. Subsequently, dividends are sticky as firms are characteristically unwilling to change dividend. This is in agreement with Campbell (2003) who stated that dividend decisions are documented as centrally vital because of increasingly major role of the finances in the firm’s general growth strategy. The objective of the finance manager should be to locate an optimal dividend policy that will augment value of the firm. It is frequently argued that the share prices of a firm tend to be condensed when there is a reduction in the dividend payments.

5.3.3 Effect of Dividend Payout Ratio on Share Prices

With regard to the effects that dividend payout ratio has on share prices it was observed that there was a significant relationship between the dividend payout ratio (DPOR) and the firm’s share price. In this regard, dividend policy is relevant to the value of share price of a listed company. From the regression and trend analysis results of the entire market it was observed that there was a positive relationship between DPOR and the market share prices though the relationship was weak. The correlation coefficient for the entire market depicted that there is a strong positive relationship between the dividend payout ratio and the share price.

Shareholders are solitary receipts of dividends; choose to have big dividend payments, all as well being equal; on the other hand, creditors choose to limit dividend payments to maximize firm’s resources that are accessible to pay back their claims. The experiential proof discussed is reliable with the sight that dividends move assets from the corporate pool to the exclusive ownership of the shareholders, which unenthusiastically affects the security of claims of debt holders. In conditions of shareholder- manager relationships, all else being the same, managers, whose return (pecuniary and otherwise) is attached to firm productivity and size, are attracted to low dividend payout levels. Gitman (1998) observed that constant dividend payout ratio is where the firm will pay a fixed dividend rate e.g. 40% of earnings. The DPS would therefore fluctuate as the earnings per share changes. Dividends are directly dependent on the firm’s earnings ability and if no profits are made then, no dividends are paid. This policy creates uncertainty to ordinary shareholders especially those who rely on dividend income and they might demand a higher required rate of return.
Low dividend payout maximizes the size of the resources under management manage, maximizes management flexibility in deciding the investments, and reduces the need to revolve to capital markets to finance investments. Shareholders aspire managerial the need to revolve to capital markets to finance investments. Shareholders, desiring managerial efficiency in investment decisions, choose to leave little optional cash in management’s hands and to force mangers to turn to capital markets to fund investments. The markets give monitoring services that authorize managers. Consequently, shareholders can use dividend policy to give confidence to managers to look after their owners’ best interests; superior payouts offer additional observing by the capital markets and more managerial restraint. According to Pandey, (2004) residual dividend policy dividend payout ratio is where dividends are paid out of earnings left over after investment decisions have been financed. Dividends will only be paid if there are no profitable investment opportunities available. The policy is consistent with shareholders wealth maximization.

The study established that stock price may be extra responsive to changing estimates of rates of return over remote time periods. Thus expanding firms although may have lower payout ratio and dividend yield, exhibit price stability. This can be because payout ratio and dividend yields serves as proxies for the quantity of predictable growth opportunities. If forecasts of profits from expansion opportunities are less dependable than forecasts of returns on property in place, firms with low dividend yield and low payout may have greater price instability. On to duration result and arbitrage effect, the dividend yield and not the payout ratio is the pertinent gauge. The rate of return result entails that both payout ratio and dividend yield matters. Dividend policies serve as a proxy for development and investment opportunities. Both the duration effect and the rate of return effect assume differentials in the timing of the underlying cash flow of the business. Rate of return effect, as discussed by Gordon (2003), is that a firm with low payout and low dividend yield may tend to be valued more in terms of future investment opportunities. As a result, Donaldson, (1961) stated that its stock price might be more receptive to altering approximations of rates of return over distant time periods. Therefore growing firms exhibit price stability.
5.4 Conclusions

5.4.1 Considerations made before Announcement of Dividend
From the findings, the study concludes that companies consider dividends paid in the previous period, the dividends to be given to the preferred shareholder, what the rival companies pay, the net earnings during the period, the amount in the reserves and the investment prospects before issuing dividends. The finding also shows that the share market is positively responsive to the dividend announcement. Therefore when the firms are considering the amount of dividend to pay they ought to consider the investment opportunities available to them whereby if the firm has good investment opportunities then it should invest the available funds first as such to increase the shareholders’ value as well as minimize the opportunities cost. Secondly, the consider the alternative sources of finances available as well as the cost whereby if the firm can access cheap alternative sources of finance then it should increase its dividend payout ratio as such to increase the share price. Thirdly, the firm should consider the loan covenants in its capital structure, since the firm has to be annual interest charges associated with the loan agreements the firm should consider the loan covenants as such to minimize the agency cost associated with the conflict of interest between the shareholders and the debt providers in a firm. Further, when the firm is developing the dividend policy it should consider the chances of losing their firm control due to firm’s dividend payout ratio decisions. Finally, the listed firms should consider the profit stability history so as to minimize the chances of incurring financial distress costs in future.

5.4.2 Relation of Share Market Prices to Dividend Announcements
The study also concludes that the share market is positively responsive to the dividend announcement such that the share market value of dividends improves in the few weeks after a high dividends announcement. There have been many studies that have found significant relationship between market prices and dividend announcement, and they have mainly shown the common characteristics on situations where the dividends are increased and earnings decreases or the vice versa, thus a conclusion can be made that the combination of dividend and news of earnings are important for purposes of explaining the reaction to the share price when the dividends are announced. Since the efficient market hypothesis stipulates that in an efficient market, all news whether good or bad, once made public the shares prices reflects them. Currently there is a significant positive relationship between the announcement of news to the public and the share prices. The quoted companies should
always declare to the public the dividend payout ratio which will satisfy the customer’s expectation and always have enough justification for a decrease in the amount of dividends announcement publicly.

5.4.3 Effect of Dividend Payout Ratio on Share Prices

It was concluded that optimal dividend policy does exist. However, the relationship between dividend policy and the share prices of the firms quoted was strong implying that dividend policy that a firm adopts determines to a large extent the market share value of the firms. It can also be concluded from the study that not all dividend pay-out policy affects the market share prices but also other determinants such as the bonus issues. The bonus issues affect negatively the market share prices since the shareholders do not regard it as an increase in their wealth but rather a reclassification of the companies earning from reserves to capital. The study can thus conclude that a company that adopts bonus issue policy will have poor performance of its shares in the market. Depending on the investors composition in the company’s shareholding the firm should investigate and develop the dividend policies which will be in favor of both the shareholders interested in capital gains or dividend yield. The dividend valuation model of stocks with growth components argued that the amount of dividend paid will determine the theoretical value of a stock. The firm should come up with dividend model which will increase the firm’s value in future. Although, the Modigliani and Miller dividend irrelevancy theory argued that the payment or nonpayment of dividend does not affect the firm’s value, the current study depicts that an increase in dividend payments increases the firms share price, thus the market capitalization increases. Therefore the quoted firms should endeavor to increase the amount of dividends payable to the ordinary shareholders of all the firms quoted in NSE.
5.5 Recommendations

5.5.1 Recommendations for Improvement

5.5.1.1 Considerations made before Announcement of Dividend
Companies should consider all pertinent issues before issuing dividends. Since the share market is positively responsive to the dividend announcement, companies should always strive to pay divided consistently for their shares to perform well at the stock exchange. Dividend policy have an effect on the share prices of the firms quoted at NSE thus, companies (firms) should pay dividends to maintain high share prices. This is pertinent with the dividend theories of bird-in-hand theory, information signaling effect theory, tax differential theory and agency theory. These theories propose that dividend policy is relevant to the value of the firm; other factors kept constant. Moreover, the random walk theory postulates that stocks value cannot be determined with certainty thus the stock price will always react to the news declared publicly. If a firm has to release information publicly then it should notify the members of the public the information that will trigger an increase in the share prices. Similarly, the firm should be consistent on how they pay their dividend. As such the investor can determine with certainty the amount he expects to receive on a particular trading period.

5.5.1.2 Relation of Share Market Prices to Dividend Announcements
It is also recommended that firms should maintain a clear and consistent dividend policy for the dividend policy to affect the value of the firm. Having established that there is a significant positive relationship between dividend announcements and share price, a similar study could be carried out on unquoted companies to see whether the same results also hold by testing the variables in this study on companies not quoted on the Nairobi stock exchange. Once the investors have received information on dividend, they will have to make decisions.
If the firms declare a dividend showing a downward trend, then most of the bear’s investors will sell the stocks in anticipation that the stock price will decrease. Due to the increased supply of the securities and no change in demand, then the share price may decrease thus the firms should announce dividends which should not create an artificial shortage or increase in share supply in the market.
5.5.1.3 Effect of Dividend Payout Ratio on Share Prices
Companies should view the payout ratio and the retained earnings ratio as the indicators of
the amount of earnings that have been ploughed back in the business. The lower the payout
ratio, the higher will be the amount of earnings ploughed back in the business and vice
versa. A lower payout ratio or higher retained earnings ratio means a stronger financial
position of the company. Since they are various guidelines on when to pay dividends, how
much dividends to pay, how to pay dividends and why pay the dividends. The dividend
payout policy for all firms should ensure that the answers to the above key questions do not
expose the firm to financial challenges nor decrease the company’s share price since the
higher the payout ratio the lower the firm’s growth opportunities. Although the current study
has depicted a positive significant relationship between the payout ratio and the share price
the quoted firms should endeavor that their dividend policies are geared towards increasing
the company’s share price while protecting the shareholders interest.

5.5.2 Recommendations for Further Studies
A similar study should be done whereby the data collection relies on primary data that is, in-
depth questionnaires and interview guide so as to complement this study. Due to the
shortcomings of regression models, other models can be used to explain the various
relationships between dividends payout ratios and the value of the firms. Since the data
collected was time series in nature, future studies should carry out time series analysis for
the data on dividend policy and the share price. A follow up study should be carried out to
investigate the moderating effect of the industry specific sector on the relationship between
share price and the dividend payout ratio. Since there are qualitative characteristics such as
the company size, age, CEO tenure, CEO duality among others which can influence the
share price apart from the dividend payout ratio a study should be carried to determine their
combined effect and their relationship with the share price.
REFERENCES


Walter, J. E. (1967). Dividend Policy and Enterprise Valuation, Belmont, California, U.S.A Wadsworth publishing company INC.


APPENDICES

Appendix I: Companies Listed in the Nairobi Securities Exchange

<table>
<thead>
<tr>
<th>Companies</th>
<th>Average Market price</th>
<th>Average Shares traded</th>
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<tr>
<td>Safaricom Limited</td>
<td>3.20</td>
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<td>607,800</td>
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<td>KenGen</td>
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<td>Barclays Bank</td>
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<td>Co-operative Bank of Kenya</td>
<td>13.00</td>
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<td>Nation Media Group</td>
<td>134.00</td>
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<td>AccessKenya Group</td>
<td>5.00</td>
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<td>Kenya Airways</td>
<td>20.00</td>
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<td>Uchumi Supermarket</td>
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<tr>
<td>British-American Investments Company ( Kenya)</td>
<td>4.60</td>
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<td>Kenya Power &amp; Lighting</td>
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<td>Housing Finance Co</td>
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<td>KenolKobil Co</td>
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<td>Centum Investment Company</td>
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<td>Kenya Re-Insurance Corporation</td>
<td>7.55</td>
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<td>British American Tobacco Kenya</td>
<td>255.00</td>
<td>12,700</td>
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<td>Sameer Africa</td>
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<tr>
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<td>E.A.Cables</td>
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<td>East African Breweries</td>
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<td>CFC Stanbic Holdings 5.00</td>
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<td>Sasini Tea &amp; Coffee</td>
<td>12.95</td>
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<td>Bamburi Cement</td>
<td>133.00</td>
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<td>Rea Vipingo Plantations</td>
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<td>Standard Chartered Bank</td>
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<td>Jubilee Insurance Co.</td>
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<td>Pan Africa Insurance Holdings</td>
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<td>ScanGroup</td>
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<td>Trans-Century Limited</td>
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<td>Olympia Capital Holdings</td>
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<td>Eaagads</td>
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<td>Express</td>
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<td>Williamson Tea Kenya</td>
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<td>Car &amp; General (K)</td>
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<td>Hutchings Biemer</td>
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<td>Marshalls (E.A.)</td>
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<tr>
<td>Kakuzi</td>
<td>68.00</td>
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Appendix II: Main Investment **Market Segment (MIMS)**

**Agriculture**
1. Rea Vipingo Ltd.
2. Sasini Tea & Coffee Ltd.
3. Kakuzi Ltd.

**Commercial and Services**
1. Access Kenya Group Ltd
2. Car & General (K) Limited
3. CMC Holdings Limited
4. Hutchings Biemer Ltd
5. Kenya Airways Ltd
6. Marshalls (EA) Limited
8. Safaricom Ltd
9. Scangroup Ltd
10. Standard Group Ltd
11. TPS Eastern Africa (Serena) Ltd
12. Uchumi Supermarkets

Finance and Investment
1. Barclays Bank
2. Centum Investment Company Ltd
3. CFC Stanbic Holdings Ltd
4. Diamond Trust Kenya Limited
5. Equity Bank Ltd
6. Housing Finance Company Limited
7. Jubilee Holdings Ltd
8. K.C.B
9. Kenya Re-Insurance Corporation Ltd
11. National Industrial Credit Bank Limited
12. Olympia Capital Holdings
13. Pan Africa Insurance Holdings Ltd
14. Standard Chartered Bank
15. Co-operative Bank of Kenya Ltd
Industrial and Allied

1. Athi River Mining Ltd
2. BOC (K)
3. Bamburi Cement Limited
4. British American Tobacco
5. Carbacid Investment Limited
6. Crown Berger Ltd
7. E.A. Cables Limited
8. E.A. Portland Cement Limited
9. E.A. Breweries Ltd
10. Eveready East Africa Ltd
11. Kenya Oil
12. K. Pow. & L.
13. KenGen
14. Mumias sugar Ltd
15. Sameer Africa Ltd
16. Total Kenya
17. Unga Ltd

Alternative Investment Market Segment (AIMS)

1. A. Baumann & Co.Ltd
2. City Trust Ltd
3. Eaagads Ltd
4. Express Ltd
5. Williamson Tea Kenya Ltd
6. Kapchorua Tea Co. Ltd
7. Kenya Orchards Ltd
8. Limuru Tea Co. Ltd
## Appendix III: Data Collection Tool

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<th>2009</th>
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## Appendix IV: Agricultural sector Market Analysis

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### Appendix V: Commercial and Services Sector Market Analysis

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<td>Marshalls</td>
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<td>0.00</td>
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## Appendix VI: Finance and Investment Sector Market Analysis

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## Appendix VII: Industrial and Allied

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