Publisher
Singh Publication
www.singhpublication.com

E-ISSN:2583-1747

Management Journal for Advanced Research

2026 Volume 6 Number 1 February

Research Article

Financial Industry

The Impact of Dividend Announcements on Shareholder Value: A Study of Select Financial Companies in India

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DOI:10.54741/MJAR/6.1.2026.284

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The financial industry is experiencing an exceptionally extensive growth, with the traditional corporations growing and new corporations entering the industry. The industry is highly diversified, comprising commercial banks, insurance companies, cooperative banks, non-banking financial institutions, mutual fund companies, and other financial entities. The question here is whether the financial sector announcements are reacted to by the investors and/or other stakeholders in the same manner as other segments are, or, on the contrary, they are impacted differently by the corporate announcements. This study is centred on seeing the effect of dividend announcements on stock returns, and more emphasis is given to the companies from the financial sector that are part of the NIFTY 100 index. This survey covers 20 financial companies from the index, which made a total of 82 announcements with regard to dividends between 2019 and 2023. The market model's event study methodology is used to test the impact of dividend announcements, and the returns that were projected are estimated by the market model.

Based on the attained data, the dividend announcements are associated with high and favourable effects on stock returns in the event period. The examination results of Average Abnormal Returns (AAR), Cumulative Average Abnormal Returns (CAAR), and the sub-event window returns also confirm that the market is already in a good mood when the announcement is made, hence the first days will show a positive market reaction. This research has, besides, found that dividends are most influential in the days right before the announcement is made. To sum up, it is concluded from the results that the market is embracing the announcement of dividends positively, which is a sign that the shareholders can gain from an abnormal return.

Keywords: dividend announcement, abnormal stock returns, financial industry, event study

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How to Cite this Article

Sogi SV, Srinivas K.T., Poornima .S, The Impact of Dividend Announcements on Shareholder Value: A Study of Select Financial Companies in India. Manag J Adv Res. 2026;6(1):61-67.
Available From
https://mjar.singhpublication.com/index.php/ojs/article/view/284

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Manuscript Received	Review Round 1	Review Round 2	Review Round 3	Accepted
2026-01-20	2026-02-07			2026-02-25

Conflict of Interest	Funding	Ethical Approval	Plagiarism X-checker	Note
None	Nil	Yes	4.16	

1. Introduction

One of the most important corporate finance choices is how much to pay out in dividends. The process of distributing dividends to shareholders has a substantial effect on the company's total worth, share value, financial stability, and development potential. A portion of the business's earnings that remains after taxes is distributed to the shareholders as a dividend. A profit organisation may have the chance to go for two choices. On the one hand, one can either not take the money out or use it for further expansion, or on the other hand, paying out cash to the shareholders would be the decision. It is a common belief among people that companies that decide not to pay out dividends have the best conditions for their growth, which consequently leads to higher stock valuation and the consequent increase in share prices. One mile that the shares have run due to the combination of the payouts that the firms have avoided and the rise of the share prices as a consequence of the payouts is not as a result of those payouts of dividends, for which the evidence has not been given in support of this assertion, as the stock's performance has improved secondary to that.

If a rational investor is given a choice between a dividend-paying and a non-paying stock, the obvious preference is for a dividend-paying stock. This is because of immediate dividend income and underappreciation in the future. According to the "Bird in the Hand" theory, the shareholders prefer dividends to capital gains because of the uncertainty that comes with future consequences (Gordon, 1962). Investors prefer the immediate cash dividends as compared with the uncertain future capital gains (Al-Malkawi, 2010). According to the "signalling hypothesis", the companies make use of declarations regarding dividends to pass the information as to expected revenues and the consistency of dividend payment. The issuance of higher dividends can be seen as an approval of the company's future profitability. A decrease in dividends is often viewed as a negative. So, the issue of paying dividends is connected with an inflow of interest to the shares of the company, which leads to a rise in share price. On the other hand, the dividend irrelevance theory states that in an environment of perfect information, declaration of dividends makes no difference in the value of a company or share prices (M-M hypothesis, 1961).

Following this, Fisher Black's (1976) authoritative pronouncement about dividend policy stands out. Going in-depth into dividend trends only presents an even more complicated puzzle with unfilled gaps. Therefore, the key question is whether the signals reported in the peer group's dividend announcements assist in boosting shareholder returns and influence share price movement. The purpose of the study is to examine the impacts of the announcement of dividends on the share prices and to depict shareholders' understanding and response to these signals.

Dividend announcements have been thoroughly researched as to their impact on share prices. To date, the sector-specific impact analysis from the announcement of dividends is still rather underdeveloped. According to an investigation by Anwar et al (2017), there exist positive abnormal returns resulting from dividend announcements in the manufacturing sector companies, which are highest one day after the announcement. Up-to-date research has largely ignored the sector-specific factors in its investigation of the impact of dividend announcements. The general response on the part of different sectors to dividend news can differ significantly. In the financial industry, regulatory changes, interest rate movements, and macroeconomic factors have a greater influence on investor response when it comes to dividend announcements of financial sector companies. The manner in which financial sector companies are approached with regard to research is often different from that of manufacturing companies. The financial sector is experiencing a rapid increase characterised by the growth of old companies and the emergence of new ones. The sector is very diversified with commercial banks, insurance companies, cooperative banks, non-banking financial institutions, mutual fund companies, and other related businesses. A major question is whether there are the same or different response patterns in financial sector companies in reacting to announcements of dividends compared to companies in other sectors, because of specific sensitivities to dividend announcements. Therefore, this research aims to fill this gap in understanding by evaluating how dividend announcements influence financial sector companies in particular. The study seeks to help shareholders and financial institutions in the same sector as they make dividend policy decisions.

It also allows investors to find out how financial sector companies respond to announcements of dividends.

2. Review of Literature

Dividend announcement returns and their correlation with stock price have been the focus of numerous papers in various geographical locations. The authors of a study, namely Wasim K et al. (2012), conducted in the Jordan Stock market, have revealed that the investors respond positively to the news about increases, reductions, and non-adjusted payments of dividends. The Chinese market, as a case in point, shows a favourable change in cash dividends (either way), says Chen et al. (2009). Gurgul et al. (2003) identified that a dividend distribution deal in Austria's financial market could not affect stock prices, while Austria's lack of dividend fluctuations had no bearing on share prices. In a different paper, Mrzygold et al. (2017) also observed that the dividend declaration in the Warsaw market gives a statistically significant result. The above-mentioned studies collectively show that the market responds positively to the announcement of dividends.

In India, Mallikarjunappa and Manjunatha (2009) found that more days produced positive than negative returns post-event, and the positive return trend increased after the event. As reported by Taneem and Yuce (2011), dividend announcements carry meaningful information and affect share prices; thus, there are higher abnormal and cumulative abnormal returns on the firm's dividend increases. Average abnormal returns were consistently high during both the event period and the announcement day, but negative during the post-event period. (Mehta et al., 2014). Also, Anwar et al. (2017) recorded that cash dividends formed positive average abnormal returns, and the highest was on the day after the announcement. Debarish et al. (2012) reported substantial abnormal returns after the dividend announcements (especially when the CAPM model was used). However, the findings of S. Saravanakumar (2011) indicate that the dividend announcements do not cause the alterations of stock returns, and no one can be expected to receive abnormal returns by outperforming.

Combined, these studies show the importance of stock prices affected by dividend announcements in line with changes towards dividend announcements, except those presented by S. Saravanakumar (2011). Yet, there is an important literature gap that deals with research that is being conducted solely on financial sector firms. As such, the purpose of this research is to explore the dividend announcement impact on stock returns of firms in the Indian financial industry.

3. Research Objectives

The present study made an attempt to examine the impact of dividend announcements on shareholders' value.

4. Hypotheses for the Study

H_{01}: The event does not cause a statistically significant deviation from expected returns during the event window.

H_{02}: The Cumulative Average Abnormal Returns (CAAR) during the event window are equal to zero.

5. Scope of the Study

The present study aims to examine the impact of the announcement of dividends on the financial sector companies, part of the NIFTY 100 Index, till August 6, 2023. There are 20 financial firms listed in the NIFTY 100 Index, which account for approximately 35.05% of the stock index's total weight. Data in this study has been analysed between 2019 and 2023, for five years. The criteria required a 71 trading day break between two announcements of dividends to ensure that the estimation period of one announcement did not coincide with the event period (window) of the previous announcement.

6. Methodology

By Application of the event study methodology proposed by Brown and Warner in 1980, the following data are analysed in this study. The study utilised an estimation window of 60 days and an event window of 21 days around the announcement day, consisting of 10 days before and 1 day after. If the announcement date is not a trading date, then the trading day following the announcement date is selected as the event day, and NSE closing prices daily over the analysis period are used to calculate the stock return. Stock prices are adjusted in the data for announced bonuses and splits.

Market return is estimated using the NIFTY 500 Index prices, as it is a more comprehensive index that gazes into the Indian stock market in various fields. Expected returns are obtained using the market model, while the statistical significance of AAR and CAAR is examined with the t-test.

Table No. 1: Table Showing List of Financial Companies' and Number of Dividend Announcements during the Period 2019-2023

Sl. No	Name of the Company	Number of Dividend Announcements
1	Axis Bank Ltd.	3
2	Bajaj Finance Ltd.	5
3	Bajaj FinServ Ltd.	5
4	Bajaj Holdings & Investment Ltd.	7
5	Bank of Baroda	2
6	Canara Bank	2
7	HDFC Asset Management Company Ltd.	5
8	Cholamandalam Investment and Finance Company Ltd.	5
9	HDFC Bank Ltd.	4
10	HDFC Life Insurance Company Ltd.	4
11	ICICI Bank Ltd.	4
12	ICICI Lombard General Insurance Company Ltd.	8
13	ICICI Prudential Life Insurance Company Ltd.	5
14	IndusInd Bank Ltd.	4
15	Kotak Mahindra Bank Ltd.	3
16	Life Insurance Corporation of India	2
17	Muthoot Finance Ltd.	5
18	SBI Cards and Payment Services Ltd.	2
19	SBI Life Insurance Company Ltd.	4
20	State Bank of India.	3
	Total	82

(**Source**: Compiled from NSE's website)

7. Results and Discussion

Average Abnormal Returns

Table No. 2: Showing Average Abnormal Return and T-statistics

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Days	AAR (%)	t-statistic	P-value
-10	-0.21	-1.19	0.24
-9	0.06	0.34	0.73
-8	0.16	0.83	0.41
-7	0.2	1.27	0.21
-6	-0.01	-0.04	0.96
-5	0.04	0.22	0.83
-4	0.15	0.9	0.37
-3	0.39	2.15**	0.03
-2	0.47	2.42**	0.02
-1	-0.22	-1.19	0.24
0	0.43	1.94*	0.06
1	0.15	0.42	0.68
2	0.16	0.96	0.34
3	0.18	0.9	0.37
4	-0.09	-0.37	0.71
5	0.09	-0.69	0.49
6	0.36	1.76*	0.08
7	0.01	0.09	0.93
8	-0.16	-1.03	0.31
9	0	-0.03	0.98
10	-0.18	-1.02	0.31

(**Source:** Author's calculations)
Note: *significant as 10 % at **significant at 5%

Interpretation: Table 2 exhibits the calculation of the average returns over 21 days, showing that dividend announcements affected stock performance; there were more positive returns observed than negative returns. Significantly high average abnormal returns in anticipation of the announcement imply that shareholders were already aware of the dividend announcement and reacted favourably well in advance. Based on the results presented in Table 2, dividend announcements are found to be associated with large average abnormal returns, and hence the null hypothesis is rejected. The event does not cause a statistically significant deviation from expected returns during the event window. On the announcement date, the return supported a positive market response that extends some support to the dividend signalling hypothesis. Climbing into a positive sentiment continues three days post-announcement, since the AAR stays high.

Incorporation of the announcement into the stock prices marks the end of possibilities for abnormal rates of return. The AAR indicates that the market mostly approved of dividend announcements.

Cumulative Average Abnormal Returns

Table No. 3: Showing the Mean Cumulative Abnormal Return and its Associated T-values are Reported

Days	CAAR (%)	t-statistic	P-value
-10	-0.21	-1.19	0.24
-9	-0.15	-0.55	0.58
-8	0	0.01	0.99
-7	0.21	0.54	0.59
-6	0.2	0.45	0.65
-5	0.24	0.49	0.62
-4	0.39	0.77	0.44
-3	0.78	1.39	0.17
-2	1.25	2.25**	0.03
-1	1.04	1.79*	0.08
0	1.47	2.26**	0.03
1	1.62	2.09**	0.04
2	1.78	2.15**	0.03
3	1.96	2.33**	0.02
4	1.87	1.94*	0.06
5	1.77	1.83*	0.07
6	2.13	2.41**	0.02
7	2.14	2.37**	0.02
8	1.99	2.18**	0.03
9	1.98	2.06**	0.04
10	1.8	1.83*	0.07

(**Source:** Author's calculations)
Note: * significant at 10% and ** significant at 5%

Interpretation: Table 3 shows the calculation of the Cumulative Average Abnormal Returns (CAAR) for the divisor of all the impact and potential return that stems from the announcement of a dividend. The CAAR tends to become higher, indicating a confident market response to the news on the dividend. Significance of CAAR from day - 2 to 10 is statistically significant, thus the observed effect is not a chance but a result of the dividend announcement. At the midpoint of the event (7th day), it is estimated that shareholders will gain maximally 2.14% with this return being statistically significant at the 5% significance level. The early importance of the CAAR at day 2 means that the market participants had observed and favourably responded to the information on the dividend before the announcement.

After the announcement, CAAR values rose, hitting 2.14% on day 7, and ended at 1.80% on day 10 when the market fully digested the details. In summary, the data suggests that stock prices experience statistically significant increases after the announcement date of the news, particularly around and following the event day – this leads us to reject the null hypothesis. The Cumulative Average Abnormal Returns (CAAR) during the event window are equal to zero.

Sub Event Windows and Returns

Table no 4: Showing Cumulative Average Abnormal Return for Sub-Event Windows and T-statistic

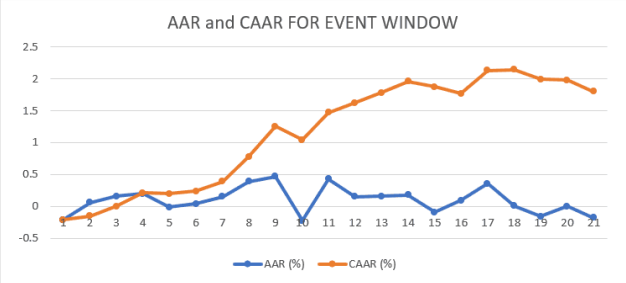
Event Window	CAAR (%)	t-statistic	P-value
(-10, +10)	1.8	1.83*	0.07
(-5, +5)	1.57	1.84*	0.07
(-3, +3)	1.56	2.57**	0.01
(-1, +1)	0.36	0.72	0.47
(-10, 0)	1.47	2.26**	0.03
(-10, +1)	1.62	2.09**	0.04
(-5, 0)	1.27	2.61**	0.01
(0, 5)	0.74	1.14	0.26
(0, 10)	0.76	1.13	0.26

(**Source**: Author's calculations)
Note: *significant at 10% and **significant at 5%

Interpretation: Table 4 represents the Cumulative Average Abnormal Return for Sub-Event Windows and the T-statistic. In order to gain a finer understanding of the influence of the event, we split the event timeframe into discrete sub-windows. The building of sub-event windows enables us to explore whether the impact of the event is increased on the days of the announcement or after its announcement. The negative pre-event windows (-10 to 0) and (-5 to 0) demonstrate a positive and significant CAAR, which argues for the meaningful impact the event had before the announcement. This suggests market anticipation. However, such event windows that only cover post-announcement days, such as (0 to 5) and (0 to 10), do not show any high positive returns. Intervals of time extending before and after the announcement, i.e., (-10 to +10), (-5 to +5), and (-3 to +3), result in positive returns but in the (-1 to +1) event window, CAAR is statistically insignificant, which indicates that the immediate effects of the event are not significant and are visible from Table 4.

This suggests that expectations are more relevant before the event than after because all event windows with more pre-announcement days produce bigger returns than those with more post-announcement days".

Figure No. 1: AAR and CAAR for the Event Window



8. Conclusion

The study examined the incidence with which dividend announcements lead to stock returns, focusing on those furnished by financial sector firms in the Nifty 100 index. The research examines 82 dividend announcements covering the period between 2019 and 2023. The stock returns' response to dividend announcements is measured through an event study methodology. By analysing Average Abnormal Returns (AAR), we find that positive AARs are reported more often than negative AARs. These findings support what was revealed by Mallikarjunappa and Manjunatha (2009). These large gains on pre-announcement days indicate that the market knew what was to come before it was announced. The Cumulative Average Abnormal Returns (CAAR) confirm this finding with a trend of overwhelmingly positive returns two days before the announcement, meaning there was market anticipation. On each day after the announcement, the CAAR remains positive and meaningful, indicating a positive market reaction. The CAAR collectively shows an unyielding upward trend of abnormal returns and potentially up to a meaningful gain of 2.14%. A similar tendency is observed when looking at Figure 1. It has been shown through analysis of sub-event windows that the direct effect of the event on day zero and thereafter (-1 of +1) is insignificant with the greatest effect having been observed in pre-announcement windows(-10 of 0) and After finding out about AAR, CAAR and returns within sub-event windows, the study concludes that announces of dividend are correlated with a clear increase in stock prices, With the information already being absorbed by the market, there is no need for any further drop in return.

In conclusion, the research shows a favourable reaction to information on dividends by investors, and there is a short-term rise in the prices of stocks of the companies involved.

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