



UNIVERSITI PUTRA MALAYSIA

**SIGNALING EFFECTS AND DETERMINANTS OF CORPORATE
DIVIDEND POLICY IN IRAN AND SAUDI ARABIA**

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GSM 2011 3

Signaling Effects and Determinants of Corporate
Dividend Policy in Iran and Saudi Arabia



By

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**Thesis Submitted to the Graduate School of Management, Universiti Putra
Malaysia (UPM), in Fulfillment for the Degree of Doctor of Philosophy**

2011

DEDICATION

Bismillahirrahmanirrahim

In the name of Allah (s.w.t.) the Beneficent and Merciful.

First, I am thankful to Allah for blessing and helping me in the life to date.

I would like to sincerely dedicate this work to my family,

To my beloved wife, Maryam, for the encouragement and love during the study.

To my wonderful children, Atefeh and Emad.

To my dear parents, my brother and my sisters, for their love, prayers and support during the life and study.

I am quite sure that without their love and supports, I would not have successfully completed my education in this stage. Allah bless all of them in their life.

Abstract of thesis presented to the Senate of Universiti Putra Malaysia in
fulfillment of the requirement for the degree of Doctor of Philosophy

**Signaling Effects and Determinants of Corporate Dividend Policy
in Iran and Saudi Arabia**

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JUNE 2011

Chairman: Professor Dr. Shamsheer Mohamad

Faculty: Graduate School of Management (GSM)

Corporate dividend policy is considered as one of the most important financial decisions that managers encounter. Researchers have listed this financial decision as one of the top ten important unresolved issues in the field of advance corporate finance (Brealey & Myers, 2005). Its importance is due to not only the amount of money involved but also the repeated nature of the decision, and interacts with other financing and investment decisions.

The previous researches of dividend assert that the dividend decisions tend to differ across countries, especially between developed and emerging capital markets. The researchers have found that dividend policies in emerging markets differed from those in developed markets, reporting that dividend payout ratios in

developing markets appeared to be lower than that in developed markets (Glen, Karmokoias, Miller, & Shah, 1995).

In recent decade, Middle Eastern financial markets have experienced a substantial development in size, activity and trading value to be considered as attractive emerging markets for foreign investors. It is notable that the stock exchanges in these financial markets are going to play more important role as investable markets in the international financial system. In this regard, firms' financial policies would be able to influence this development process by affecting on investment returns and risks involved. Therefore, from this prospective, firms' dividend decisions are taken into account as one of the most important financial policies by investors and policy makers. Although so far, limited empirical research have been made on the topic in this region and further research need to be done to clarify the various aspects of the decision.

The present study investigates the determinants of dividend policy as well as the directional effect of dividend announcements on the stock price in two large Middle Eastern countries Iran and Saudi Arabia. The study employs panel data of 193 listed companies comprising 133 firms in sample of Iran together with 60 firms in sample of Saudi Arabia over the period of 1997 to 2008. The previous pattern of dividend payments documents that the majority of listed firms in both markets are willing to pay out high dividend, indicating the important role of dividend policy in the markets.

The first objective of the study is to investigate the directional effects of dividend announcements on the stock returns. Using Risk Adjusted Market model the parameters of α and β are estimated to calculate the abnormal returns around the announcement date. The t-statistic is used to test the significance of the abnormal returns and cumulative abnormal returns for short-term and long-term window around the event date. The results confirm the revaluation effect of dividend change announcements in both markets. In sample of Iran, the daily abnormal return on the announcement day appears to be around 0.2 percent, with significant t-statistics for dividend increase category. Positive abnormal returns are created by dividend increase announcements while the announcements of dividend decrease are followed by negative abnormal returns. Results of no-change in dividend are similar to the case of dividend increase by positive abnormal return around the event day. The cumulative abnormal returns show significant effect of dividend increase announcements especially over the pre-event periods.

In Saudi Arabia, the daily abnormal returns vary from -0.2 percent for dividend decreases to 0.3 percent for dividend increases. The effect of dividend decrease announcements is stronger than that for dividend increases on stock price. The results of no-change in dividend, similar to the case of Iran, create positive abnormal return on the event day but not significant. The cumulative abnormal returns show a strong negative pattern for dividend decrease over both pre-event and post-event periods. While for dividend increase category, the cumulative abnormal returns are positive only over pre-event periods.

The results confirm that dividend change announcements have informational content in both markets, but the effects of dividend changes announcements in Iran are stronger than that in Saudi Arabia especially for dividend increase category. Therefore, the signaling hypothesis of dividend appears to be supported in both markets by positive reactions to the announcement of dividend increases and negative reactions to dividend decreases in both countries.

For the second objective, some static and dynamic regression models are employed respectively to investigate the determinants of firms' dividend policy in both markets. At the first stage, the study applies static regression models such as pooled OLS regression and GLS model to estimate the parameters, and then several diagnostic tests were used in the study. The results of the specification tests show that for both samples Fixed Effect model is the best static model.

Secondly, the dynamic analysis is conducted using a combination of GMM approach and instrumental variable. Under the GMM model, the Arellano and Bond's (1991) estimator is used to estimate the dynamic determinants of dividend policy. The results suggest that firms' dividend policy can be highly influenced by several determinants. The findings indicate that for sample of Iran, market to book value, firm size, profitability, lagged payout ratio, market share, and majority ownership positively affect dividend payout ratio, whereas beta coefficient is associated with dividend payout ratio with largest negative effect. But for sample of Saudi Arabia the variables of GDP growth rate, lagged payout ratio, free cash flow, retained earnings, majority ownership, market share, and oil price positively determine dividend payout ratio, while beta coefficient, market to book value, and

leverage are negatively associated with payout ratio. This study also established a stylized fact that besides firm specific variables, some macroeconomic variables such as GDP growth rate, interest rate, and oil price influence firms' dividend policy in Saudi Arabia.

In summary, dividend decision is one of the most important financial decisions for listed companies in Iran and Saudi Arabia. The findings of this study show that firms' dividend policy in selected markets, is affected by various firm characteristics as well as economic factors, and the two most important determinants of dividend decision are market risk (Beta) and market to book value (Tobin's Q) in both markets. This study reveals the signaling effects of dividend change announcements, in which the announcements of dividend increase create positive abnormal returns while the announcements of dividend decrease result in negative abnormal returns. The findings support the signaling hypothesis of dividend for both Middle Eastern countries.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai
memenuhi keperluan untuk ijazah Doktor Falsafah

**Kesan Pengisyaratan dan Faktor Penentu Dasar Dividen Syarikat
di Iran dan Arab Saudi**

Oleh

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Dasar dividen syarikat adalah dianggap sebagai pertimbangan kewangan paling penting yang ditemui oleh pihak pengurusan Syarikat. Para penyelidik telah menyenaraikan pertimbangan kewangan ini sebagai salah satu daripada sepuluh isu penting yang masih belum dapat diselesaikan di peringkat tinggi kewangan syarikat (Brealey & Myers, 2005). Isu ini penting bukan sahaja kerana jumlah wang yang terlibat tetapi juga kerana sifat keputusan yang berulang-ulang dan berkait dengan keputusan pembiayaan dan pelaburan lain.

Penyelidikan dividen sebelum ini menunjukkan bahawa keputusan dividen adalah berbeza di tiap-tiap negara, khususnya antara pasaran modal maju dan membangun. Para penyelidik mendapati bahawa dasar dividen di pasaran negara-negara membangun adalah berbeza dari dasar dividen di pasaran negara maju.

Mereka melaporkan bahawa nisbah pembayaran dividen di pasaran membangun di dapati lebih rendah berbanding pasaran negara maju (Glen, Karmokoias, Miller, & Shah, 1995).

Dalam dekad terakhir ini, pasaran kewangan Timur Tengah yang boleh dianggap sebagai pasaran baru muncul yang menarik bagi pelabur asing, telah mengalami perkembangan besar dari segi saiz, aktiviti dan nilai perdagangan. Perlu direkodkan bahawa bursa saham di pasaran kewangan akan memainkan peranan yang lebih penting sebagai pasaran yang boleh dilaburi dalam system kewangan antarabangsa. Dalam keadaan ini dasar kewangan syarikat berupaya mempengaruhi proses pembangunan yang akan memberi kesan pada pulangan pelaburan dan risiko terlibat. Oleh itu dari sudut ini, keputusan dividen syarikat boleh dianggap sebagai satu dasar kewangan yang paling penting oleh pelabur dan pembuat dasar. Walaubagaimanapun setakat ini, kajian empirik yang dibuat dalam topik ini untuk kawasan ini adalah terhad dan penyelidikan lebih lanjut perlu dilakukan untuk memperjelas pelbagai aspek keputusan.

Kajian ini meneliti faktor-faktor penentu dasar dividen serta pengaruh arah pengumuman dividen pada harga saham di dua buah negara besar di Timur Tengah iaitu negara Iran dan Saudi Arabia. Kajian in menggunakan data panel daripada 193 buah syarikat tersenarai iaitu 133 buah syarikat dari Iran dan 60 buah syarikat dari Saudi Arabia untuk tempoh 1997 hingga 2008. Pola pembayaran dividen terdahulu menunjukkan bahawa majoriti syarikat yang berdaftar di kedua-dua pasaran sedia membayar dividen yang tinggi, menandakan betapa pentingnya peranan dasar dividen di pasaran.

Objektif pertama kajian ini adalah untuk menyiasat pengumuman dividen keatas pendapatan saham. Menggunakan model Pasaran Risiko Dilaraskan parameter α dan β dianggarkan untuk mengira pulangan abnormal sekitar tarikh pengumuman. T-statistik digunakan untuk menguji signifikan pulangan abnormal dan pulangan abnormal kumulatif untuk tettingkap jangka pendek dan jangka panjang di sekitar tarikh peristiwa. Keputusan mengesahkan kesan penilaian semula pengumuman perubahan dividen di kedua-dua pasaran. Di dalam sampel Iran, pulangan abnormal harian pada hari pengumuman kelihatan berada sekitar 0.2%, dengan t-statistik yang signifikan untuk kategori dividen meningkat. Pulangan abnormal positif berlaku pada pengumuman kenaikan dividen sedangkan pengumuman penurunan dividen adalah diikuti oleh pulangan abnormal negatif. Keputusan dividen tidak berubah adalah serupa dengan kes kenaikan dividen berdasarkan pulangan abnormal positif pada hari peristiwa. Pulangan abnormal kumulatif menunjukkan pengaruh pengumuman kenaikan dividen yang signifikan terutama sepanjang jangkamasa pra-peristiwa.

Di Saudi Arabia, pulangan abnormal harian berubah dari -0.2% untuk dividen menurun dan 0.3% untuk dividen meningkat. Kesan pengumuman penurunan dividen lebih kuat daripada kesan pengumuman peningkatan dividen kepada harga saham. Keputusan dividen tidak berubah seperti kes di Iran, menghasilkan pulangan abnormal positif tetapi tidak signifikan pada hari peristiwa. Pulangan abnormal kumulatif menunjukkan pola negatif yang kuat untuk penurunan dividen sepanjang jangkamasa pra-dan pasca-peristiwa. Sedangkan untuk kategori

peningkatan dividen, pulangan abnormal kumulatif adalah positif hanya pada jangkamasa pra-peristiwa.

Hasil kajian mengesahkan bahawa pengumuman perubahan dividen mempunyai kandungan maklumat di kedua-dua pasaran, namun kesan pengumuman perubahan dividen di Iran lebih ketara dari di Saudi Arabia khususnya untuk kategori dividen meningkat. Oleh kerana itu, hipotesis pengisyaratan dividen adalah disokong di kedua pasaran berdasarkan reaksi positif terhadap pengumuman peningkatan dividen dan reaksi negatif terhadap pengumuman penurunan dividen di kedua-dua negara.

Untuk objektif kedua, beberapa model regresi statik dan dinamik digunakan untuk menyiasat faktor penentu dasar dividen syarikat di dalam kedua-dua pasaran. Pada peringkat pertama, kajian ini menggunakan model regresi statik seperti regresi OLS dan model GLS dikumpulkan untuk menganggarkan parameter, dan kemudian beberapa ujian diagnostik digunakan dalam kajian ini. Hasil ujian spesifikasi menunjukkan bahawa model Kesan Tetap adalah model statik terbaik untuk kedua-dua sampel.

Kedua, analisis dinamik dilakukan dengan menggunakan kombinasi pendekatan GMM dan pembolehubah penting. Berdasarkan model GMM, estimator Arellano dan Bond (1991) digunakan untuk menganggarkan faktor penentu dasar dividen yang dinamik. Keputusan kajian menunjukkan bahawa dasar dividen syarikat sangat dipengaruhi oleh beberapa faktor penentu. Penemuan kajian menunjukkan

bahawa untuk sampel Iran, nilai pasaran berbanding nilai buku, saiz syarikat, keuntungan, nisbah pembayaran dividen tertinggal, agihan pasaran, dan pemilikan majoriti mempengaruhi nisbah pembayaran keluar dividen secara positif, sedangkan koefisien beta adalah berkaitan dengan nisbah pembayaran keluar dividen dengan kesan negatif yang terbesar.

Namun untuk sampel dari Saudi Arabia pembolehubah kadar pertumbuhan KDNK, nisbah pembayaran dividen tertinggal, aliran tunai bebas, perolehan tersimpan, pemilikan majoriti, agihan pasaran, dan harga minyak menentukan nisbah pembayaran dividen, secara positif sedangkan koefisien beta, nilai pasaran berbanding nilai buku, dan leverage kesemuanya adalah berkait secara negatif dengan nisbah pembayaran dividen.

Penyelidikan ini menghasilkan satu fakta bahawa selain pembolehubah syarikat yang spesifik, beberapa pembolehubah ekonomi makro seperti kadar pertumbuhan KDNK, kadar faedah, dan harga minyak boleh mempengaruhi dasar dividen syarikat di Saudi Arabia. Rumusannya, keputusan dividen adalah salah satu keputusan kewangan yang paling penting bagi syarikat tersenarai di Iran dan Saudi Arabia.

Penemuan kajian ini menunjukkan bahawa dasar dividen syarikat di pasaran terpilih, akan dipengaruhi oleh pelbagai ciri-ciri syarikat serta faktor ekonomi, dan dua faktor penentu yang paling penting untuk keputusan dividen ialah risiko pasaran (Beta) dan nilai pasaran berbanding nilai buku (Tobin's Q) di kedua-dua

pasaran. Kajian ini mendedahkan kesan pengisyaratan pengumuman perubahan dividen, di mana pengumuman kenaikan dividen mengakibatkan pulangan abnormal positif sedangkan pengumuman penurunan dividen mengakibatkan pulangan abnormal negatif. Penemuan kajian ini menyokong hipotesis pengisyaratan dividen untuk kedua-dua negara Timur Tengah.



AKNOWLEDGMENT

It is my pleasure to express sincere gratitude to Professor Dr. Shamsheer Mohamad, my supervisor and chairman of the committee, for his support and encouragement throughout my doctoral research. Undoubtedly, words cannot express my appreciation for his helpful guidance and contribution to my work. He has provided me with great knowledge of academic research in the field of finance. I will always be indebted to him for all he has done.

I would be also grateful for helps and supports of other committee members; Professor Dr. Annuar Md Nassir and Associate Professor Dr. Taufiq Hassan Chowdury. Their valuable comments and encouragement were beneficial for me in the preparation of this thesis.

I should also thank Professor Dr. Arfah Saleh, dean of Graduate School of Management (GSM), Universiti Putra Malaysia, for providing us with useful academic programs and facilities in GSM. Other especial thanks goes to other staff members at GSM who have had friendly support during the study.

Last but not least, I wish to express my deepest appreciation and love to my dear parents and forever indebted to them in my life. My especial thanks would be for my wife Maryam, and my children, Atefeh and Emad for many sacrifices they have made on my behalf. Without their support and patience, I would not have accomplished my education to date successfully.

I certify that an examination committee met on 1st JUNE 2011 to conduct the final examination of Abdorreza Asadi on his Doctor of Philosophy thesis entitled "Signaling Effects and Determinants of Corporate Dividend Policy in Iran and Saudi Arabia" in accordance with Universiti Putra Malaysia (Higher Degree) Act 1980 and Universiti Pertanian Malaysia (Higher Degree) Regulation 1981. The committee recommends that the candidate be awarded the relevant degree. Members of Examination Committee are as follows:

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