

Effect of Dividend Per Share on Share Prices After the Initial Public Offer (IPO) for Quoted Companies in Kenya

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Abstract: *The stock market reacts differently to various factors ranging from economic, political and socio-cultural. The stock prices of quoted companies in Kenya are affected either positively or negatively by a number of factors occurring within or without the economic system. These prompted the researcher to investigate the effect of dividend per share on share prices after the initial public offer (IPO) for quoted companies in Kenya. The study specifically focused on investigating the effect of expected future earnings on share prices after an IPO, investigating the effect of level of growth rate on share prices after an IPO and investigating the effect of earnings news on share prices after an IPO. The study was conducted through a descriptive survey design whereby data was gathered from secondary sources through thorough examination of financial performance records of the quoted companies listed at Nairobi Security exchange. The data was then analyzed and evaluated for usefulness, consistency, credibility and adequacy through content analysis. The findings obtained from the study were presented in form of Tables and graphs. The recommendations were made from the findings. The analysis of the data was done using the SPSS version twenty one and for secondary data questionnaires was used to get further information from company executives. From the analysis, an Overall the R-Square of all the regressions was generally high denoting that the strength of association between the variables was high meaning that the share price is dependent on Earnings per share, Dividends per share, GDP and the exchange rate. These variables were seen to be statistically significant since the p value was less than a point five. The study revealed that there was indication of some strong relationship from variables such as earnings per share, exchange rates and dividends per share. The study recommends that firms should take keen consideration on earnings per share, dividends per share, exchange rate and Real GDP in order to enhance the share prices of firms listed in the NSE.*

Keywords: Dividends per share, expected future earnings, Level of growth rate, Earning news, Share price, initial public offer (IPO), and quoted companies in Kenya

1. Introduction

An Initial Public Offer (IPO) is a vital step for firms, providing them access to the public equity market for the first time (Lewellen, 2010). Indeed, it is the first sale of stock by a private company to the public and the consequential listing on a stock exchange. Going public allows firms to raise and access funds necessary to accelerate growth in order to achieve market leadership (Ernst and Young (2010)). In addition, the liquidity created by going public provides initial investors, owners, founders and shareholders with an opportunity to collect on their investment. Further more, an IPO can facilitate future acquisitions, higher valuations, debt reductions and public profile enhancement (Blum, 2011).

According to Kipngetich et al (2011), Initial Public Offers (IPO) involves problems regarding price discovery due to uncertainties regarding aggregate demand and the quality of the issuer. Bensveniste and Spindt (2007) argue that issuers can feign themselves to investors as being of high reputation than they are. Derrien (2005) concurs that pricing of IPOs can be an uphill task due to obscurity of discovering an appropriate comparable firm. Research available mainly in developed countries has documented the extent of underpricing of IPOs without identifying the main factors involved in setting the IPO offer price. Many researchers (Cornelli, (2004); Ljungqvist, (2006) & Purnanandan and Swaminathan (2005), have presented evidence that IPOs are underpriced. Underpricing refers to the percentage

difference between the offer price and the first day of trading at the NSE.

In the Vision 2030 policy paper, the capital market is expected to play a key role towards making Kenya a developed country. Part of this growth will be spurred by the listing of private and government owned firms in NSE giving the general populace chance to own equity in such firms and participate in their management and profitability. This underscores the need for investors to understand the worth of investing in both the short and long term as well as the investment climate. Capital Markets Authority (CMA), which regulates and supervises NSE, through its investor education campaign, has succeeded in increasing the level of participation in the capital markets by proactively engaging in outreach programs.

Dealing in shares and stocks in Kenya started in the 1920s during colonial times. The market was informal and based on a "gentleman's agreement" as there were no rules and regulations governing such trading. At the time, stock broking was conducted as an incidental business by professionals in other areas such as accountants, auctioneers, lawyers and estate agents. In 1951, an estate agent by the name of Francis Drummond established the first professional stock broking firm. He also approached the then Finance Minister of Kenya, Sir Ernest Vasey and impressed upon him the idea of setting up a stock exchange in East Africa. The two approached London Stock Exchange officials in July of 1953 and the London officials accepted to recognize the

setting up of Nairobi Stock Exchange as an overseas stock exchange. In 1954, NSE (now Nairobi Securities Exchange) was constituted as a voluntary association of stock brokers registered under the Societies Act (NSE Website).

After almost 10 years, in 2006, there was resurgence in IPOs with Kenya Electricity Generating Company (KenGen) over-exceeding market expectations by being oversubscribed and earning a premium from its first day of trading. This IPO ushered in a new era for NSE with use of the Central Depository and Securities Corporation (CDSC). The CDSC Cooperates a central depository system, provides central clearing, settlement and depository services for securities listed at NSE. After Ken Gen, the other IPOs were not received with as much enthusiasm until the Safaricom Limited (Safaricom) one (with sale of 10 billion ordinary shares at KShs 5.00 per share and listing of 40 billion ordinary shares) was advertised in 2008 and literally everyone wanted a stake in it. This led to banks and financial institutions coming up with innovative funding mechanisms to capitalize on this demand. This issue was oversubscribed leading to numerous refunds.

2. Statement the Problem

The short and long term performance of newly issued equity has been of significant interest to investors. Benefit shown ever to individual investors are not always clear when it comes to returns offered by the price used in the investment of shares in the stock market. Researchers abroad have suggested that investing in new ordinary equity results to cascading returns (high initial returns in the short term and inferior performance over the long term), Ritter (1991), Aggarwal, Leal and Hernandez (1990). Capital markets efficiency is concerned with the relationship between information and share prices and in terms of the reaction of stock prices to the flow of information. The nature of emerging markets is such that prices cannot be assumed to reflect all available information. Where investors cannot correctly interpret information that is released and as such there is great potential for prices to move in a manner not justified by the information available, this raises important questions regarding the efficiency of the stock market and the effect of such conditions on stock returns.

Research available mainly in developed countries has documented the extent of under pricing of IPOs without identifying the main factors involved in setting the IPO offer price. Sunde and Sanderson (2009) in their study Determinants of Share Price in the Zimbabwe Stock Exchange argued that the market price of the stocks is affected by economic, political and social factors. What is needed in pricing an IPO is a way to engage in serious price discovery in setting the price at an IPO. The level of initial returns reaching unprecedented peaks and long-term under performance of the share price, the search for the reasons of these anomalies is still unresolved Durukan (2002).

Most Kenyan studies have focused on under-pricing and performance of IPOs such as Ngahu (2006) on book value per share issue price and first trading day prices of IPOs at NSE, Cheluguet (2008) on investor's demand for IPOs and first day performance: evidence from NSE, Ndatimama

(2008) on performance of IPOs, Leshore (2008) on medium-term performance of IPOs, Simiyu (2008) on pricing and performance of initial public offering: a comparison between state owned enterprises and privately owned enterprises at NSE and Wachira (2010) on the determinants of the success of IPOs among listed companies and Kipng'etich et al (2011) on determinants of IPO pricing in Kenya.

Despite the above studies, not much has been done on determinants of equity prices after IPO. Kenyans are expressing a growing interest in investing in equities, especially shares, at the Nairobi Security Exchange (NSE) after the initial listing. Past Initial Public Offerings (IPOs) including the Kenya Electricity Generating Company (KenGen) attracted massive subscriptions and huge financial investments. This study sought to investigate effect of dividend per share on share prices after the initial public offer (IPO) for quoted companies in Kenya and it will result to more companies being listed and the growth of these companies will increase its growth in terms of shares leading to the improvement of the company performance in Kenya.

General objective of the Study

To determine the effect of dividend per share on share prices after the initial public offer (IPO) for quoted companies in Kenya

Specific objectives of the Study

- 1) To determine the effect of expected future earnings on share prices after the initial public offer (IPO) for quoted companies in Kenya.
- 2) To explore the effect of level of growth rate on share prices after the initial public offer (IPO) for quoted companies in Kenya.
- 3) To establish the effect of Earning news on share prices after the initial public offer (IPO) for quoted companies in Kenya

3. Theoretical Framework

Random Walk Theory

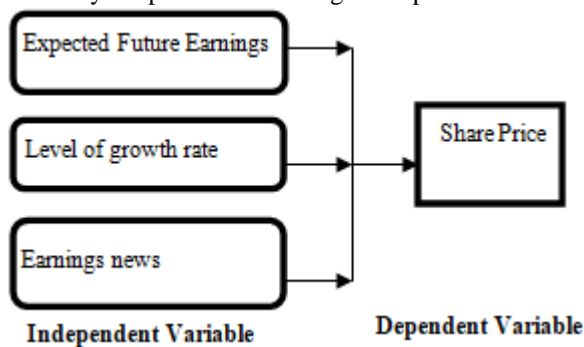
In the case of Random walk, the stock market context does not mean, neither should it be taken to imply, that the price movements are whimsical and chaotic (Mlambo, 2003). All it means is that period-to-period price changes should be statistically independent and unforecastable if they are properly anticipated. Price movements are a perfectly rational response to information but since there is no reason to expect new information to be non-random, price changes based on this information is supposed to be random and uncorrelated to any observable trend (Fama, 1970). The theory argues that the share price movements are independent of one another and unrelated. This happens in an efficient market where the current prices of securities represent unbiased estimates of their intrinsic values. The random theory holds that the prices move in a random manner hence, it is not possible to predict future prices. The price movement, whether up or down, occurs as a result of new information and since investors cannot predict the kind of new information (whether good or bad), it is not possible to predict future price movement.

The random walk theory clearly conflicts with technical analysis. The theory says that previous price changes or changes in returns are useless in predicting future prices, which implies that the work of a technical analyst is unnecessary. According to Fisher and Jordan (1995); Mlambo (2003), the random walk theory is a special case of a more general efficient market hypothesis and the two positions complement each other.

Lumby (1994), asserts that the theory of market efficiency and stock prices behavior is inseparable. In Lumby (1994), the efficient market has been defined as a market where prices of a company's shares (or other financial securities) rapidly and correctly reflect all relevant information as it becomes available. No undervalued securities exist in such a market hence, the share prices can be relied upon to correctly reflect the true economic worth of the shares. Jensen (1978), points out that a market is efficient with respect to information if it is impossible to make abnormal economic profits by trading on the basis of that information. This theory addressed the technology variable.

4. Conceptual Framework

The study adopted the following conceptual framework:



Source: Author 2017

Conceptual framework

5. Earnings per share

The revenue earned by a company after meeting cost of production, then interest, depreciation and tax belongs to the equity share stockholders. The current EPS figures and the individual shareholders' expectations of future growth relative to that of other companies also have an impact on the share price Kang (2008). EPS is calculated by dividing the earnings with the weighted number of ordinary shares. Panel counteraction methods were used by Chang, Chen, Su and Chang (2008) to investigate the relationship between stock prices and earnings-per-share (EPS). They also considered whether stock prices respond to EPS under different levels of growth rate of operating revenue. The empirical result indicated that the cointegration relationship existed between stock prices and EPS in the long-run. They also found that for firm with a high level of growth rate, EPS has less power in explaining the stock prices; however, for the firm with a low level of growth rate, EPS has a strong impact in stock prices.

To investigate whether current period earning divided by stock price at the beginning of the stock market period, current period dividend divided by stock price at the beginning of the stock market period, prior dividend divided by stock price at the beginning of the stock market period and the reverse of stock price at the beginning of the stock market period are relevant to explain stock market returns in Iran, Ebrahimi and Chadegani (2011), used cross-section, pooled data and panel data regression models. The results indicate that in some years, shareholders take special interest in dividends and also the variable prior dividend divided by stock price at the beginning of the stock market period affects stock return. They also found that there is a significant relationship between current period earning divided by stock price at the beginning of the stock market period and stock return. The implication is that the results theoretically support the existence of relationship between earning, dividend and stock return.

The relationship between earnings figures and stock returns Dimitropoulos and Asteriou (2009). They carried out investigation of the above relationship in the context of the Greek capital market. They stated that previous studies resulted in controversial results regarding the usefulness of models which were using earnings levels or earnings changes as the explanatory variable. In an introductory context, the study examines the earnings-return relation applying four models as proposed by Kothari and Zimmerman (2010). The results indicate a significant value relevancy of accounting earnings prepared under the Greek GAAP.

Their financial variables for the study are Earning per Share (EPS), Dividends per Share (DPS) and Price to Earnings ratio (P/E). Eventually, the fuzzy linear regression model for examining the relationship between DPS, EPS and P/E variables and stock price of Iran Khordo Company has been presented. The empirical results of this research indicate that there is a positive and significant relationship between Earning per Share (EPS) and stock price of the company. However, there is a negative and significant relationship between Dividends per Share (DPS) and Price to Earnings ratio (P/E) of the said company.

Umar and Musa (2013) studied the relationship between stock prices and firm earning per share (EPS) which appears to be contestable like any other performance measures. The results, based on 60 listed companies in Shanghai Stock Exchange for 2011, reveal that positive relationship exists between accounting information and stock price, but the significant degree varies. The result further reveals that earnings per share and return on equity have the most significant correlation.

6. Research Methodology

The study was descriptive and quantitative in nature of the assessment of determinants of share price performance after the initial IPO for quoted companies in NSE. The population of this study consisted of the companies listed at the Nairobi security exchange of Kenya since 2006 to 2016. Our sample was drawn from quoted companies from 2006-2016. This was done because after almost 10 years of no IPOs as the

NSE there was resurgence in IPOs with eight companies being listed at NSE in a span of five years. This study used secondary data which was obtained from the financial statements of the companies, Central Bank of Kenya and Kenya National Bureau of Statistics. Secondary data collection sheets was used since the firms are manageable and due to availability of the financial statements in the Nairobi security Exchange website. It was then summarized in an excel data sheet for the analysis. The data were sourced from financial reports, library, company website, journals as well as publications relevant to the firms listed at the NSE. Descriptive statistics was used to analyze the quantitative data. The findings were presented using tables, graphs and pie charts.

7. Results and discussions of the findings

Earnings per share

The study sought to explore the effect of earnings per share on share prices after the initial public offer (IPO) for quoted companies in Kenya and after retrieving the data from the organization website the findings were as discussed using Tobin's Q is book value of total assets plus market value of equity minus book value of equity divided by book value of total assets. The results showed that the earnings per share had a mean of .65 with a minimum of -.47, a maximum of .38, skewness 0.453 and kurtosis of +2.045. The study concurs with the findings of Ebrahimi and Chadegani (2011), used cross-section, pooled data and panel data regression models to show establish the influence of earnings per share on the share price. The results indicate that in some years, shareholders take special interest in dividends and also the variable prior dividend divided by stock price at the beginning of the stock market period affects stock return. They also found that there is a significant relationship between current period earning divided by stock price at the beginning of the stock market period and stock return.

Kengen

The data collected was for the period 2006 to 2016 on four variables. Share price of stock is the dependent variable while Earnings per share, Dividends per share, real gross domestic product and exchange rate were the independent variables. Kenya Electricity Generating Company or simply KenGen is a state-owned company, the largest power producing company in Kenya producing about 80% of the electricity consumed in the country. The company was founded in 1998 when it was separated from the Kenya Power and Lighting Company (KPLC). The KenGen shares were listed on the Nairobi Stock Exchange since 2006. The predicted model from Table 4.3 below was: $SP = -386.244 + 1.876 \text{Earnings per share} + 3.676 \text{Dividends per share} + 0.000000186 \text{GDP} + 1.567 \text{Exchange rate}$. The R-Square, the coefficient of determination, is an overall measure of the strength of association between the dependent and independent variables. The overall p value was less than 0.05 (0.000) and it was deduced that the group of independent variables when used together reliably predict the dependent variable therefore showed a significant statistical relationship. This also addressed the ability of the particular independent variables to predict the dependent variable. The

ability of each individual independent variable to predict the dependent variable was addressed below based on the model coefficients in Table 4.3 below. For independent variables which were statistically significant, their coefficients were significantly different from zero and were in the equation.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.853	0.7276	0.7251	0.0064

Table 4.1 above presented the regression model goodness of fit on the independent variables. A Correlation value of 0.853 was established depicting that the independent variable (Earnings per share, Dividends per share, GDP, Exchange rate) had a very good linear relationship with share price. An R-square value of .728 was established depicting that the relationship was very strong and that the independent variables influences 72.8% of the share price.

Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1655670.68	4	237856	10.56	.000 ^a
	Residual	2239897.34	1230	24556		
	Total	3895568.02	1236			

ANOVA analysis was conducted to determine the significance of Earnings per share, Dividends per share, real gross domestic product and exchange rate on the Share price of stock at Kengen the in the regression model. An F-significance value of less than 0.001 was established depicting that the predictor variables had a high significance in the model (confidence level) ($p < 0.05$).

Model Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t-value	Sig.
	B	Std. Error	Beta		
(Constant)	-386.244	78.55		-45.34	0.001
Earnings per share	1.876	0.344	0.085	1.676	0.011
Dividends per share	3.676	0.896	0.092	3.456	0.002
GDP	1.86E-08	0	0.0345	0.768	0.367
Exchange Rate	1.567	0	0.145	2.567	0.003

The constant was statistically significant as its coefficient was different from zero and its p value was less than 0.05 (0.001). For the Earnings per share, the coefficient (parameter estimate) was 1.876 so, for every percent increase in the earnings per share, a 1.876 shilling increase in share price was predicted, holding all other variables constant. This variable was statistically significant since the p value is less than 0.05 (0.011). For every shilling increase in Dividends per share, there was a 3.676 shilling increase in the predicted share price, holding all other variables constant. This variable was statistically significant since the p value was less than 0.05 (0.002). As for GDP, every shilling increase caused a 1.86×10^{-8} shilling increase in

predicted share price, holding all other variables constant. This variable coefficient was not statistically significantly different from zero and its p value was more than 0.05 (0.36) hence did not significantly predict share price and was removed from the predictor model. For every shillings increase in Exchange rate, there was 1.567 shilling increase in the predicted share price, holding all other variables constant. This variable was statistically significant since the p value is less than 0.05 (0.003). Based on the above explanations, the predictor model for Kengen was therefore rewritten as : $SP = -386.244 + 1.876\text{Earnings per share} + 3.676\text{Dividends per share} + 1.567\text{Exchange rate}$ meaning that the share price after initial public offer is dependent on earnings per share, dividend per share and exchange rate. The study findings are in agreement with Dimitropoulos and Asteriou (2009) who carried out an investigation of the relationship between earnings figures and stock returns in the context of the Greek capital market. They stated that previous studies resulted in concurring results regarding the usefulness of models which were using earnings levels or earnings changes as the explanatory variable.

8. Summary of the Findings

Creation and strengthening of an independent Public institution to monitor dividend manipulation, stabilization of Interest rates, EPS insurance against share losses for firms in Kenya just like the Central Bank does to the Banks in Kenya. This can be done through creation of an oversight committee.

9. Conclusions

From the above results, exchange rates, earnings per share and dividends per share seemed to have a slightly larger significance in determination of share prices after initial public offer which could have been influenced by the fact that it incorporates all companies quoted at NSE. The GDP had a less significant effect on share prices after initial public offer.

10. Recommendations

The study recommends that the Government of Kenya strengthen the CMA (Capital Markets Authority) to come up with mitigation measures to control the external factors that interfere with share prices with a possible measure to cushion NSE from international monetary fluctuations; Control and moderation of interest rates especially the strategic ones that can be used in determination of share price behavior

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