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EFFECT OF DIVIDEND POLICY ON SHARE PRICE OF COMMERCIAL BANK IN NEPAL

Bidhya Pandey

ABSTRACT

This study has examined the effect of dividend policy on share price of commercial banks in Nepal. The descriptive and causal comparative research designs have been adopted for the study. The data of 13 commercial banks for the period FY2014/15 to 2019/20 have been analyzed using regression model. The regression results revealed that the sampled commercial has a significant effect of dividend policy on their share price. The study shows significant positive effect of DPS,DPR,PER, and EPS on share price(MPS). The insignificant result of bank size indicates that bank size cannot be considered an influencing variable for share price.. This study concludes that Nepalese commercial banks need to increase their dividends to help induce their share prices.

Keyword: Earning per share ,Price to earning ratio , Bank size, Market per share

Background of the study

A dividend is a portion of a company's profits and retained earnings that it distributes to its stockholders. When a company makes a profit, a portion of it is set aside as retained earnings, and the rest is either distributed as a dividend or reinvested in the company. Dividends are a significant source of income for investors. Profits are used to pay dividends. As a result, when a company declares a dividend, it means the company is doing well and is stable. It attracts more investors, which increases the demand for that stock, causing the price to rise.

Market Price per Share (PS) is the cost of purchasing a share on the Nepalese stock exchange (NEPSE). The market price per share is determined by several factors such as dividend payout ratio, earnings per share, dividend per share, firm size, firm growth, liquidity position, and some other macroeconomic variables. In this study, dividend payout ratio and earnings per share are considered. Investors who want to maximize their dividend income buy stock in that company. When purchasing equity shares on the secondary market in developing countries like Nepal, investors primarily consider the firm's profitability. Because dividends paid to shareholders are one of the best indicators of profitability, it is widely assumed that dividends play a significant role in determining the market price of a corporate share (Khadka, 2012).

Bhandari and Pokharel (2012), stated that only a few companies pay dividends in Nepal, and many others do not pay a consistent dividend. Some businesses have never paid dividends to shareholders. Dividend on share is a key indicator that demonstrates a bank's performance and thus attracts investors. Investors should research the dividend policies of banks before investing in the stock market. However, because of fluctuations in Nepal's commercial banks' dividend policies, investors are unable to forecast future cash flow from cash dividends. Companies that have increased their dividend have seen their stock price rise, whereas companies that do not pay or have reduced their dividend have seen their stock price fall. As a result, the dividend affects the company's stock price. Adhikari (2063) conducted research and discovered that there were discrepancies in the dividend payments made by Nepal's commercial banks. There was no consistency in commercial banks' dividend payout ratios. As a result, he advised investors to consider the high profit margins of companies when purchasing shares.

The purpose of this study is to investigate the impact of dividend policy on the share price of a commercial bank in Nepal. This study examines how dividend policy affects bank share price using a robust sample, and the findings will be useful to investors, policymakers, shareholders, and management of the selected commercial bank. It is also necessary for the government's policymakers, controllers, monitors, and supervisors to regulate commercial banks in Nepal.

Rational of the study

The finding of the study will be helpful for the investors for the investment decision along with policymakers, shareholders and management of the commercial bank. it is expected that many people, particularly those working in the banking industry, such as bankers, financial analysts, bank managers, commercial bank management, and investors, will benefit greatly. The findings of this study will benefit researchers and academics because they will provide a theoretical and empirical framework for understanding how dividend policy affects the share price of commercial banks in Nepal.

Research gap

Nepal's capital market is in its early stages of development, and Nepalese investors have made significant investments in newly established companies without conducting a thorough analysis of those companies, particularly in the financial sector. This trend

will continue until investors are satisfied with the decisions made by these companies' management. Dividends are the most motivating factor for an investor to invest in the stock of various companies. In Nepal, when a company earns a lot of earning, it retains more of it, and when it doesn't, it declares a big dividend to protect its image in the capital market. Even if dividends affect the firm's value, unless management knows exactly how they affect value, there is not much that they can do to increase the shareholders' wealth. As a result, management must understand how the dividend policy affects the firm's market valuation or stock price. Although previous research has revealed the effect of dividend policy on share price of commercial banks in Nepal, no studies had examined the effect of multiple dividend policy variables on share price using new data at the time of the study with increase of observation of the study as a result, the purpose of this research is to fill that gap.

Research question

Is there significant effect of Dividend per share (DPS), earning per share (EPS), Dividend payout ratio (DPR), Price earning per share (PER) and size on share price of commercial bank in Nepal ?

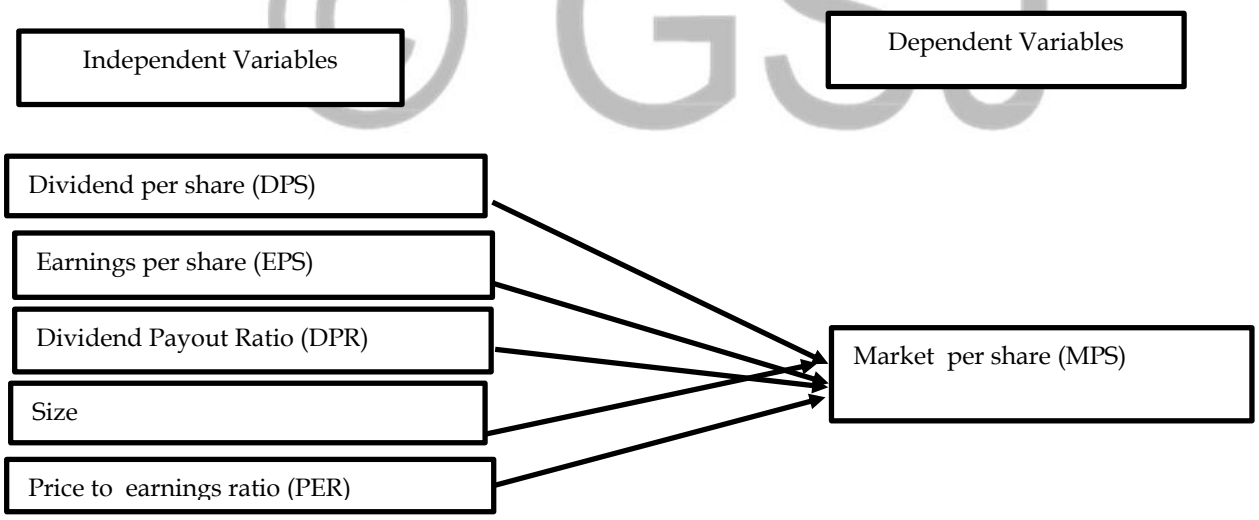
Research objectives

To measure the relationship between dividend policy and share price of commercial bank in Nepal.

To examine the effect of Dividend per share (DPS), earning per share (EPS), Dividend payout ratio (DPR), Price to earnings ratio (PER) and size on share price (MPS) of commercial bank in Nepal.

Research framework

Figure 1.1: Research framework for the study



Definition of variables

Dependent variables

Market per share (MPS)

Stock values can fluctuate minute by minute due to changes in buying and selling pressure. These changes make deciding which market price to use as a measure of independent variables difficult. In the current analysis, the market price is the closing stock price at the end of the bank's fiscal year.

Independent variables

Dividend per share (DPS)

Dividend per share (DPS) is the sum of a company's declared dividends for each ordinary share outstanding. It is calculated by dividing net income available to common stockholders by the number of outstanding common shares. DPS is an important metric for investors because the amount a company pays out in dividends directly translates to shareholder income. A rising DPS can also indicate that a company's management believes its earnings growth can be sustained. Joshi (2012) discovered a significant positive effect of dividends on the firm's share price. Asadi (2013) likely discovered a significant positive effect of dividend on the firm's share price. In the absence of the clientele effect, if the company pays larger cash dividends, the market value of its shares will rise(Bhattarai, 2016).

Earnings per share (EPS)

Earnings per share (EPS) is calculated by dividing a company's net profit by the number of common shares outstanding. EPS is a widely used metric for estimating corporate value because it shows how much money a company makes for each share of stock it owns. A higher EPS indicates greater value because investors will pay more for a company's shares if they believe the company's profits are greater than its share price. Baral and Pradhan (2022) and Dhungel (n.d) conducted the research and found positive significant impact of EPS on share price of commercial bank. According to Islam, Khan, Choudhory, and Adan (2014), the share price does not move as quickly as earnings per share. Although it is an important factor, other factors should also be considered when purchasing stock.

Dividend Payout Ratio (DPR)

The dividend payout ratio is the percentage of earnings distributed to shareholders as dividends. The payout ratio can also be used to determine the long-term viability of a dividend. Companies are extremely hesitant to reduce dividends because it can lower stock prices and reflect poorly on management's abilities. On a per-share basis, it is commonly calculated by dividing annual dividends per common share by earnings per share (EPS). Gautam (2017) conducted research on Dividend policy and Share Price Volatility: A case of Nepalese Commercial Banks, using regression model and conclude that dividend payout ratio is negatively related to stock price. Similarly, Sharif, Ali, and Ali Jan (2015) discovered that Dividend Payout Ratio has a significant positive relationship with stock price.

Size of the bank

Size is an important financial tool that is used to represent the bank's volume in a variety of ways. Large banks, on the other hand, generally provide better banking services to customers and borrowers than smaller banks. Banks, due to their larger size, generally hold a stronger and more dominant position in the stock market. Large bank shares are actively traded on the stock exchange, providing investors with greater liquidity and marketability. As a result of the temptation to buy shares of large banks, the market

price of its shares rises. The total assets scaled in natural logarithm are used to determine the size of the banks in this study. Pradhan and Dahal (2018) research study find out that there is a significant positive relationship between firm size and share market price.

Price to earnings ratio (PER)

The P/E ratio is an independent variable in this study. It is concerned with comparing market value to earnings per share. The price earnings ratio shows how much each share's price covers its earnings. It indicates whether the stock price of a company is appropriately valued, undervalued, or overvalued. In general, companies with a high P/E ratio indicate that investors expect higher future profit growth than companies with a low P/E ratio. These studies, like Malhotra and Tandon (2013) and Almumani (2014), discovered a significant positive correlation between price-earnings ratio and firm stock price.

Hypotheses

Based on the above reviews and research framework following hypotheses are formulated:

H1: There is significant effect of dividend per share (DPS) on share price.

H2: There is significant effect of earning per share (EPS) on share price.

H3: There is significant effect of price to earning ratio(PER) on share price.

H4: There is significant effect of bank size on share price.

H5: there is significant effect of dividend payout ratio on share price.

Emperical Reviews

Bhattarai (2016) investigated the impact of dividend payments on the stock prices of Nepalese commercial banks. Using secondary data from six commercial banks over a seven-year period (2010 to 2016), the researcher discovered a significant positive relationship between share price and dividend payment, and the researcher concludes that dividend payment positively affects the share price of Nepalese commercial banks.

Baral and Pradhan (2018) investigate the impact of dividend policy on the share price of a Nepalese commercial bank. The study was based on the collection of cross-sectional data from ten commercial banks. Data are gathered from Nepalese commercial banks listed on the NEPSE from fiscal years 2012/13 to 2016/17. The articles conclude that, aside from DPR, other factors such as EPS and P/E ratio have a positive relationship with stock price. In the case of top gainer commercial banks, P/E is the most powerful factor influencing share price, while EPS, P/E ratio, and DPR all have a positive impact on stock price. In the case of a top loser bank, DPR is the most powerful factor influencing share price.

Malhotra and Tandon (2013) investigated the factors that influence stock prices in the context of 100 companies listed on the National Stock Exchange (NSE). For the period 2007-2012, a sample of 95 companies was chosen, and a linear regression model was used. The findings revealed that a firm's book value, earnings per share, and price earnings ratio have a significant positive relationship with its stock price, whereas dividend yield has a significant inverse relationship with its stock price.

Almumani (2014) examined the factors influencing the market price of shares of listed banks on the Amman Stock Exchange from 2005 to 2011 and discovered that stock prices were positively related to ratios such as EPS, P/E ratio, and book value of shares. The relationship between DPS and share market price was found to be insignificant.

Joshi (2012) examines the impact of dividends on stock price in Nepal. The stock price was used as the dependent variable, with four other variables serving as explanatory variables: Dividend Per Share (DPS), Retained Earnings Per Share (REPS), Lagged Price Earnings Ratio (P/E ratio), and Lagged Market Price Per Share (MPS). This study's overall conclusion is that dividends have a significant effect on market stock price in both the banking and non-banking sectors.

Gautam (2017) conducted the research study and concluded that Dividend Policy and Share Price Volatility: A Case of Nepalese Commercial Banks, using a regression model, concluded that dividend payout ratio is negatively related to stock price volatility.

Velankar (2016) examines the Effects of Earnings per Share and Dividend Payout Ratio on Stock Price: A Study on Selected Public Sector Banks in India; using a regression model, researcher discovered that Earnings per Share has a significant impact on market price per share.

Shrestha (2015) revealed that dividend per share is positively related to market price per share. Similarly, dividend yield is positively affected by size. Bhandari and Pokharel (2012) concluded that the dividend policy of Nepalese commercial banks is not consistent. The dividend policy followed by Nepalese commercial banks is not fully explained by either residual theory or stable theory. With the development of financial institutions in Nepal, they must adhere to a solid dividend policy so that investors can forecast the stock market and make sound investment decisions.

Research design

The main objective of this study is to Examine the effect of dividend policy on the share price of a Nepalese commercial bank. For the purpose of achieving the study's goal, the research mostly uses historical and descriptive data. This study's research design is a descriptive and causual and comparative research design. For this research, secondary data were used. Secondary data is gathered and examined from a variety of reports published by representative commercial banks and the NRB. After analyzing the information gathered, the research is finished with appropriate conclusions and suggestions. The conclusions are entirely based on the data and information that is currently accessible.

Nature and Sources of Data

This study examines a panel data set of 13 commercial banks from FY2015 to 2020. The research is based on numerical data. Data for this study were gathered from the Nepal Rastra Bank (NRB) website, annual reports of commercial banks, and other sources. The banks selected for the study are: Everest Bank Ltd., Global IME Bank, Himalayan Bank, Kumari Bank, Nepal SBI Bank, NIC Asia Bank, NMB Bank, citizen bank, sanima bank, Prime bank, Laxmi bank, Siddhartha Bank and Prime bank. The required data are retrieved from the annual report of respective banks.

Data analysis tools and technique

Financial and statistical approaches were used to examine the effect of independent variables on dependent variables. For data calculation and analysis, Microsoft Excel and eviews software were utilized. The regression model was used to evaluate the effect of independent variables on dependent variables.

Population and Sample

The entire Nepali commercial bank is the study's complete population. In Nepal, there are now 26 commercial banks in operation. 78 observations from 13 commercial banks whose six fiscal years' financial reports are available on their websites were selected as a sample for the analysis.

Methods of Data Analysis

The data collected was statistically analyzed using software such as E-views. Several tools were used to draw conclusions from the collected data:

Descriptive Statistics
Multiple regression analysis

Mainly statistical tools such as descriptive analysis has been used for the purpose of generating findings. Apart from these analyses in some of the variables, mean, standard deviation, minimum, maximum, Pearson correlation coefficient is calculated for findings of the conducted research.

Multiple Regression Analysis

Some tests relating to the quality of the adjustment would be necessary prior to the development of the regression. In general, there are two approaches to analyzing panel data.

- The method of pooled ordinary least squares (OLS).
- Model with fixed or random effects.

Breusch- Pagan Test

Breusch Pagan LM test is a parametric test used to determine whether or not pooled OLS regression model fits the regression analysis. The test uses the following null and alternative hypothesis:

Hypothesis for Breusch-Pagan Test

H0: Pooled OLS method is appropriate
H1: Pooled OLS method is not appropriate

If p-value is less than 0.05, H0 is rejected. When pooled OLS is not significant, further test has to be done to identify whether fixed effect or random effect model to apply.

Hausman Specific Test

The Hausman specification test is used to select a suitable method for models (fixed or random effects approach). The null hypothesis of the Hausman specification test indicates that the random effects approach is preferable. In contrast, the alternative hypothesis fixed effect approach is more appropriate.
The following multiple regression model is used to achieve the results of predefined objectives.
The relationship between bank profitability (ROA) and the variables related to credit risk management is the focus of the first model, as shown by the following.

$$MPS= \beta0 +\beta1DPS+\beta2EPS+\beta3DPR+\beta4SIZE+\beta5PERt+e \quad \text{(I)}$$

where,
MPS = Market price per share
DPS= Dividend per share
EPS= Earnings per share
DPR= Dividend payout ratio
PER= Price to earnings ratio
$\beta0$= constant,
e = error term,
$\beta1$, $\beta2$, $\beta3$, $\beta4$, $\beta5$ are coefficients

4.1 Descriptive Statistics

This section examines descriptive statistics for selected variables. This section focuses on the data's behavior in relation to the central tendency. Following tables summarize thev ariables' characteristics are shown by revealing the statistical mean, median, maximum, and minimum values, standard deviation, and number of observations.

Table 1: Descriptive summary of the dependent variable

Particular	MPS
Mean	6.099
Median	6.054
Maximum	8.127
Minimum	5.225
Std. Dev.	0.545
Observations	78

Source: Author's calculations from Eviews 12 SV, 2022

Table 1shows that 78 observations for dependent variables were recorded for thirteen Nepalese commercial banks from 2012 to 2022 MPS ranges from 5.22% to 8.17%, with an average of 6.099%. The standard deviations of the variable is 0.545.

Table 2: Descriptive summary of the independent variables

Particular	DPS	DPR	EPS	SIZE	PER
Mean	17.534	0.748	23.513	25.283	21.428
Median	16.00	0.732	23.065	25.330	19.150
Maximum	70	1.862	43.030	26.335	83.940
Minimum	0	0	10.150	24.344	11.150
Std. Dev.	10.177	0.313	7.542	0.448	10.574
observations	78	78	78	78	78

Source: Author's calculations from Eviews 12 SV, 2022

Table 4.2 shows that there are 78 observations for independent variables recorded over the period 2012 to 2022 or thirteen commercial banks of Nepal. Mean of dividend per share of bank is 17.534 It fluctuates between 0 3 to 70% with standard deviation 10.177. The mean of dividend per share is 0.748. It fluctuates between 0 to 1.862 with standard deviation 0.313. Average earning per share is 23.513 it fluctuates between 10.150 to 43.030 with standard deviation 7.542 Average price to earning ratio is 21.42, which fluctuates between 11.15 to 83.94 with standard deviation 10.574 Average size of bank is 25.283 it fluctuates between 24.344 to 26.335 with standard deviation 0.448.

4.2 Correlation Matrix

The research has total six variables with two dependent and five independent variables which are determining their effect on bank profitability. The correlations are shown following in table no 4.3

Table 3: Correlation matrices of variables

Correlation probability	MPS	EPS	DPS	DPR	SIZE	PER
MPS	1					
EPS	0.7686 (0.00)	1				
DPS	0.598 (0.000)	0.559 (0.00)	1			
DPR	0.143 (0.211)	-0.025 (0.826)	0.7618 (0.000)	1		
SIZE	-0.060 (0.600)	-0.093 (0.415)	-0.150 (0.0188)	-0.077 (0.499)	1	
PER	0.7925 (0.000)	0.319 (0.004)	0.520 (0.000)	0.277 (0.014)	0.001 (0.991)	1

Source: Author's calculations from EViews 12 SV, 2022

The correlation matrix and multicollinearity diagnostics for profitability measurements, the number in parathesis shows the P-value and other show the value of correlation. Result indicates that EPS, DPS, DPR and PER has positive and size has negative relationship with MPS.

Gujarati (2007) state that the problem of multicollinearity exists if the correlation between independent variables is greater than 0.8. Here, all of the correlation coefficients between the independent variables are 0.8. This impression indicates that multicollinearity issues are not present. As a result, the model's independent variables are best suited for regression analysis.

4.4 Normality Test

In statistics, the Jarque–Bera test is a goodness-of-fit to test of whether sample data have the skewness and kurtosis matching a normal distribution. The test is named after Carlos Jarque and Anil K. Bera. An assessment of the normality of data is a prerequisite for many statistical tests because normal data is an underlying assumption in parametric testing.

Table 4: Normality test

Test	Jarque-Bera Value	Probability
	0.811	0.666

Source: Author's calculations from Eviews 12 SV, 2022

A normality test is used to determine whether sample data has been drawn from a normally distributed population. The table 4.4 shows the normality test of the data used for the study. As the probability shows the value of 0.666which greater than 0.05 level of significance, we can say that the data are normally distributed.

4.6 Estimation method

Panel data analysis is used in the study because it is more effective than pure cross-sectional or pure time series data in locating and quantifying effects that are indistinguishable from one another. Panel data, rather than cross-sectional or time series data, enables the development and testing of more complex behavioral models. Panel data analysis employs a variety of approaches. These techniques include pooled ordinary least squares, fixed effects, and random effects. The pooled ordinary least squares method is nothing more than an ordinary least squares method. This method ignores the panel nature of the dataset because it does not account for variations between populations over time. Furthermore, because of the heterogeneity between the error term and the independent variables, the estimates derived from this measure are severely biased. Because the pooled ordinary least squares model is unable to adequately capture the panel character of the dataset, the fixed effects and random effects models are advantageous and beneficial. To choose between fixed and random effects, we can use a Hausman test, where the null hypothesis is that the random effect model is better than the fixed effect model and the alternative hypothesis is that the fixed effect model is better than the random effect model.

4.7 Regression Analysis

The regression model is used to predict and estimate the effect of the independent variable on the dependent variable.

$MPS= \beta 0 +\beta 1DPS+\beta 2EPS+\beta 3DPR+\beta 4SIZE+\beta 5PERt+e…$

Table.5: Breush Pagan LM test

	Cross-section	Time	Both
Breush Pagan LM Test	0.404	12.150	12.554
P-value	(0.524)	(0.0005)	(0.0004))

Source: Author's calculations from Eviews 12 SV, 2022

First Breusch-Pagan test is conducted for equation (1), results shows that P-value is 0.524 which is greater than 0.05 level of significance which accept null hypothesis and it suggests that pooled OLS method is appropriate.

Table 6: Panel regression results

Variables	Coefficients	Std. Error	T-Statistics	Prob.
EPS	0.059	0.004	12.045	0.000
DPS	-0.025	0.006	-4.260	0.0001
DPR	0.595	0.154	3.852	0.0003
Size	-0.036	0.036	-1.020	0.3108
PER	0.0354	0.0018	18.84	0.000
C	4.877	0.911	5.351	0.000

Model Summary	
R-squared	0.939
Adjusted R-squared	0.935
F-statistic	223.25
Prob (F-statistic)	0.0000
Durbin-Watson stat	1.394

Source: Author's calculations from Eviews 12 SV, 2022

As illustrated in the model in Table 4.7 , among the variables, Market price per share (MPS),Dividend per share(DPS), Earnings per share (EPS),Dividend payout ratio (DPR), Price to earnings ratio (PER) is found to have statistically significant effect on market price per share (MPS). The coefficient of EPS,DPR and PER found to be positive reveals that having positive significant effect at the level of 1% (p-value <0.01). It is determined that 1% change in EPS will results 0.059% change in MPS, similarly, 1% change in DPR and PER will result 0.59% and 0.035% change in MPS. The result shows that DPS has negative significant effect on MPS at the level of 1% level which indicate 1% increase in DPS will results 0.025% decrease in MPS but size shows negative insignificant relation with MPS.

R- squared for the regression is 0.939which implies that the explanatory variables in the current study can explain 0.939 of the variations in the share prie, MPS. The remaining 0.07 percent of variations of the share price of commercial banks under investigation can be explained by other factors not included in the model. Furthermore, regarding the statistical significance of the model it's P-value=0.0000 is less than 1% level, indicating strong statistical importance of the estimated model, which extends the reliability and validity of the model.

Summary of hypothesis

Table 7: Summary of hypothesis

Hypothesis	P-value	Remarks
H1: There is significant effect of dividend per share (DPS) on share price.	0.0001	Accept
H2: There is significant effect of earning per share (EPS) on share price.	0.000	Accept
H3: There is significant effect of price to earnings ratio(PER) on share price.	0.000	Accept
H4: There is significant effect of bank size on share price.	0.3108	Reject
H5: there is significant effect of dividend payout ratio on share price.	0.0003	Accept

Conclusion

Different dividend policy variables are used in this study to determine the effect on the share price of Nepalese commercial banks. The pooled OLS technique is used in this study to determine whether there is a significant relationship between DPS,DPR,PER,EPS, and Size and share price (MPS). Correlation analysis is used to investigate the existence of a relationship between DPS,DPR,PER,EPS and Size and share price (MPS) based on findings. The Breusch-Pagan LM test was used to determine which method to use based on the value of the data used, and the Jarque-Bera test was used to ensure that the data was normal.

According to the findings of this study, the sampled commercial has a significant effect of dividend policy on their share price. The significant positive results of DPS,DPR,PER, and EPS demonstrate this. The insignificant result of bank size indicates that bank size cannot be considered an influencing variable for share price. As a policy recommendation, all commercial banks in Nepal should increase their dividends to help induce their share prices. Furthermore, the study's findings are based on 78 observations; there is room for more in-depth analysis using larger sample sizes and sophisticated econometric methods. Furthermore, the study is limited to thirteen bank specific independent variables; thus, additional research on the topic should be conducted using other bank specific, industry related, and macro level variables to generate more reliable results. Regardless, it is hoped that this study will be useful to academics as a source of knowledge for future research, as well as policymakers in the banking sector in pushing share prices and market indexes.

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