

## Dividend Announcements and Stock Market Reaction: Further Evidence

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**Abstract:** This paper examines stock market reactions to announcements of dividend increases and decreases in Bursa Malaysia. The data consist of all the firms that announced dividend increases or decreases from 2001 to 2005. Using an event study approach, the evidence shows that dividend increase announcements are greeted positively by investors, while there is some evidences suggesting investors react negatively prior to dividend decrease announcements. The observations are then separated into the magnitude of dividend change and income change. This paper also separates the observations into government linked companies (GLCs) and non GLCs. For the income-increase group of GLCs and non GLCs, the buy-and-hold abnormal return is positive and statistically significant in the post-announcement period.

**Keywords:** Bursa Malaysia, dividend announcement, market reaction

### Introduction

This paper examines stock market reactions to announcements of dividend increases and decreases in Bursa Malaysia (formerly known as Kuala Lumpur Stock Exchange). Prior research on developed markets indicates a positive correlation between dividend changes and stock market reaction. Dividend increase is considered as good news while dividend decreases as bad news. Two of the most discussed theories of dividend behaviour are information signaling hypothesis and agency theory. The information-signaling hypothesis argues that since there is an information asymmetry between management and shareholders, the only way for the management to signal future prospects is by changing the dividend payout. According to the agency problem perspective, when the management increases dividends, it reduces the possibility of the management misusing the firm's free cash flow. Empirical evidence strongly supports this argument and thus confirms the theory.

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