



MENTOR | The Journal of Business Studies

JBS

Faculty of Commerce and Management, Eastern University, Sri Lanka

Dividend Policy and Shareholders' Wealth: Evidence from Listed Food, Beverage and Tobacco Companies in Sri Lanka

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ABSTRACT

The aim of this study was to investigate the impact of dividend policy on shareholders' wealth, with a specific focus on companies in the food, beverage, and tobacco sectors listed in the Colombo Stock Exchange (CSE). Data were collected from the annual reports of 27 selected companies over a five-year period, spanning from 2017 to 2021.

To examine this impact, the study used Dividend per Share, Dividend Pay-out Ratio, and Dividend Yield as explanatory variables. Additionally, Market Price per Share served as a proxy for shareholders' wealth. The study also considered Firm Size and Financial Leverage as control variables to assess their impact of dividend policy on shareholders' wealth. To analyze the data, the study utilized correlation and panel data regression analysis. Before conducting the regression analysis, the Variable Inflation Factor (VIF) test was employed to check for any multicollinearity issues among the explanatory variables. The results showed no significant problems of multicollinearity.

Regarding the panel data regression, three different models were used: pooled Ordinary Least Squares (OLS), fixed-effect, and random-effect models. After conducting the analysis, the fixed-effect model was determined to be the most appropriate model for explaining the impact of dividend policy on shareholders' wealth. The results from the fixed-effect model indicated that Dividend per Share positively impacts on shareholders' wealth. Results supported the signaling theory. As per the signaling theory if Dividend per share increases it will reveal the company's future prospectus. Therefore investors want to invest in that company's shares. As a results that company's share prices increases thus share holders' wealth maximize. In contrast, Dividend Yield exhibited a negative relationship with shareholders' wealth. Companies may face difficulties in gathering sources of financing during the pandemic situation. So if the companies pay more dividend to their shareholders, mostly they will have to depend on the long term loans for their sources of financing. As a result the companies need to pay higher interest, which will decrease the shareholders' wealth by reducing the earning per share. These findings will assist to the better management of the companies by taking proper decisions on dividend policies. Also it aids the shareholders as well as the investors to make informed choices regarding their wealth.

Keywords: Dividend Policy, Dividend per Share, Shareholders' Wealth, Colombo Stock Exchange

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1. Introduction

The main objective of financial management is to maximize the value of organizations for both owners and shareholders (Pandey, 1979). In this context, financial managers in an organization should make decisions that help maximize shareholders' wealth. Three crucial dimensions of financial management are investment decision, financing decision, and dividend decision. The dividend policy, specifically, is a critical decision that determines how much of the organization's earnings should be distributed to shareholders as dividends and

how much should be retained for reinvestment in the business (Al-Malkawi, 2008). This decision directly impacts shareholders' wealth.

The Colombo Stock Exchange (CSE) is the primary stock market in Sri Lanka and plays an integral role in the country's economy. Investors are attracted to the stock market when they have knowledge about shareholders' value and its determinants. This, in turn, helps in developing the Sri Lankan economy by increasing investments in the capital market. Dividend policy is a key factor that determines the value of shareholders in an organization.

"Dividend policy is the strategy utilized by a company to determine the distribution of its profits to shareholders. It signifies the proportion of remaining net earnings allocated to shareholders. Research conducted by Baker and Powell (1999), Hussainey, Mgbame, and Chijoke-Mgbame (2011), and David. (2022) has consistently highlighted the substantial impact of dividend policy on both share price volatility and firm valuation. Various theoretical frameworks have been devised to elucidate the connection between dividend policy and fluctuations in share prices. This relationship has been investigated across different countries and time periods...". Numerous studies have been conducted on dividend policy in relation to shareholders' wealth, such as those by Priyan and Nyabakora (2022), Nambukara and Peries (2020), and Dilshani and Abeywardhana (2018). However, the findings of these studies have been inconclusive, and a comprehensive understanding of the relationship between dividend policy and shareholders' wealth is still needed.

Thus, the primary objective of this study is to investigate the impact of dividend policy on shareholders' wealth in the Food, Beverage, and Tobacco companies listed on the Colombo Stock Exchange over the period from 2017 to 2021. The research question of this study is: "What is the impact of dividend policy on shareholders' wealth of Food, Beverage, and Tobacco companies listed on the CSE?"

By addressing this research question, the study seeks to contribute to the existing knowledge on dividend policy and its impact on shareholders' wealth in the context of Sri Lanka's capital market. The findings of this study can have practical implications for financial managers, investors, and policymakers, providing them with valuable insights for making informed decisions related to dividend policy and maximizing shareholders' wealth.

2. Literature Review

There are many theories about dividend policy. The Modigliani and Miller (M&M) theory of dividend policy says that dividend payment does not affect the value of the company. However signalling theory of dividend policy suggests that company's dividend policy gives a signal about the company's future prospects, which means when the company announces the dividend payment that promotes to invest in that company. Agency theory suggests inefficient decision making results from the conflict of interest between a company manager's and its shareholders.

Shareholders Wealth

Shareholders' wealth refers to shareholders' equity, which is the difference between assets and liabilities. It represents the value that shareholders have in a particular company. Several studies have found a significant impact of dividend policy on shareholders' wealth (Priyan and Nyabakora, 2022; Nambukara and Peries, 2020; Dilshani and Abeywardhana, 2018).

Dividend Per Share

Dividend per share is defined as the total amount of dividends attributed to the number of ordinary shares outstanding. It helps investors determine how much income they will receive from the company on their shares. Previous studies have shown mixed findings regarding the impact of dividend per share on share

price volatility among Sri Lankan firms. Some studies found no significant impact (Dissanayake and Wickramasinghe, 2016), while others found a significant positive relationship between dividend per share and shareholders' wealth in Sri Lankan non-financial companies listed on the Colombo Stock Exchange (Yogendrarajah et al., 2022).

Dividend Pay-out Ratio

Dividend pay-out ratio indicates the percentage of a company's earnings after tax paid out to shareholders. It signals to investors that a business is earning enough to distribute dividend payments, which helps instill confidence in their investments. Previous studies have yielded mixed findings regarding the relationship between dividend pay-out ratio and shareholders' wealth in Sri Lankan non-financial companies listed on the Colombo Stock Exchange. Yogendrarajah et al., (2022) has found that there is insignificant relationship between Dividend Pay-out ratio and shareholder's wealth in Sri Lankan non-financial companies listed in Colombo Stock Exchange. Kengatharan, and Ford (2021) found Dividend yield shows significant positive impact on share price volatility Nevertheless, Harshapriya (2016) had found significant negative relationship between dividend pay-out and stock price volatility in her study carried out in Sri Lanka.

Dividend Yield

Dividend yield is the ratio between dividend and the current market price per share. It represents the percentage of a company's share price that is paid out in dividends each year. Previous studies have shown mixed findings regarding the relationship between dividend yield and shareholders' wealth in Sri Lankan non-financial companies listed on the Colombo Stock Exchange, with some studies finding a significant negative relationship and others finding a significant positive relationship (Yogendrarajah et al., (2022)). However Kengatharan and Ford (2021) found significant positive relationship between dividend yield and share price volatility. Farrukh et al. (2017) found significant positive relationship between dividend yield and share price among Pakistan firms.

Firm Size

Firm size is considered as a control variable in this study and can be measured through various factors such as the number of employees, total assets, and total sales revenue. In this study, firm size is measured by the natural logarithm of total assets. Previous studies have shown varying relationships between firm size and shareholders' wealth in Sri Lanka and globally. Yogendrarajah et al. (2022) used firm size as control variable in their study and found there is significant positive relationship between firm size and shareholder's wealth and Iqbal et al. (2014) had found Firm size has significant positive impact on shareholders wealth of selected manufacturing industries in Pakistan.

Financial Leverage

Financial leverage is also used as a control variable in this study and represents the financial ratio between total debt and total assets of a particular firm. It indicates how much of the borrowed finance is used for financing the firm's assets. Previous studies have shown mixed findings regarding the relationship between financial leverage and shareholders' wealth. Ali and Waheed (2017) have found Positive significant impact of leverage on share price volatility in Pakistan. But, Yogendrarajah et al. (2022) in Sri Lanka found insignificant relationship between leverage and shareholders' wealth.

Many researches regarding to dividend policy had been carried out before the Covid pandemic situation in developing and developed countries. Even though the economy of Sri Lanka has faced miserable challenges due to the outbreak of Covid. So in this occasion there is a need to carry out several researches to find out

the financial decisions and its impact on the firms' value. As dividend decision plays a prominent part in financial decision, this topic has been chosen to fulfil the research gap.

Based on the above analytical review of empirical literature, following hypotheses are formulated to examine the impact of dividend policy on share holders' wealth of Food, Beverage, and Tobacco companies listed in the Colombo Stock Exchange in Sri Lanka.

H₁- Dividend per Share's significant impact on Shareholders' Wealth.

H₂- Dividend Pay-out Ratio's significant impact on Shareholders' Wealth.

H₃- Dividend Yield's significant impact on Shareholders' Wealth.

3. Research Methodology

This study adopts a deductive approach, and secondary data is collected from the annual reports of companies. The target population of the study is Food, Beverage, and Tobacco companies listed in the Colombo Stock Exchange in Sri Lanka as of March 2023. Out of the total population of 48 companies, those that didn't distribute any dividends to shareholders within the sample period and companies with unavailable data were excluded from the study. The final sample consisted of 27 firms for the years 2017-2021. Secondary data was collected from the annual financial reports of the selected firms, available on the CSE's website. The variables and their measurements are presented in Table 1.

Table 1. Variables and their measurements

Variables	Indicators	Measurements
Dividend Per Share (DPS)	Total amount of dividends attributed for number of ordinary share outstanding.	Total Dividend Paid/ Number of Ordinary Shares Outstanding
Dividend Pay-out Ratio (DPR)	The percentage of dividend payment to company's earnings after tax paid	Dividend / net income after tax
Dividend Yield (DY)	Ratio between dividend and current market price per share	Annual Dividend Per Share/ Market price Per Share
Firm Size (FS)	Natural logarithm of total assets.	Log of Total Assets
Financial Leverage (FL)	Financial ratio between total debt and total asset	Total Debt/Total Assets
Shareholder's Wealth (MPS)	Shareholders' equity or difference between assets and liabilities /It means it is a value that shareholders' have in the particular company	Log of Market Price Per Share at the end of the Year

Models Specifications

The following regression model has been formulated to analyze the impact of dividend policy on Shareholders wealth of Food, Beverage and Tobacco companies listed in CSE. This study examined 27 firms with 135 observations using panel data collected from 2017 to 2021 to determine the relationship between dividend policy and shareholders' wealth.

Pooled OLS Model

$$MPS_{it} = \alpha + \beta_1 DPS_{it} + \beta_2 DPR_{it} + \beta_3 DY_{it} + \beta_4 FS_{it} + \beta_5 FL_{it} + \varepsilon_{it}$$

Fixed Effect Model

$$MPS_{it} = \alpha + \beta_1 DPS_{it} + \beta_2 DPR_{it} + \beta_3 DY_{it} + \beta_4 FS_{it} + \beta_5 FL_{it} + u_{it}$$

Random Effect Model

$$MPS_{it} = \alpha + \beta_1 DPS_{it} + \beta_2 DPR_{it} + \beta_3 DY_{it} + \beta_4 FS_{it} + \beta_5 FL_{it} + u_{it} + \varepsilon_{it}$$

In the equation,

MPS_{it} is the log of Market Price per Share of firm i at time t .

DPS_{it} is the Dividend per Share of firm i at time t

DPR_{it} is dividend pay - out ratio of firm i at time t .

DY_{it} is Dividend Yield of a firm i at time t

FS_{it} is Log of total assets of firm i at time t .

FL_{it} is Firm Leverage of a firm i at time t

α Is coefficient of intercept

$\beta 1, \beta 2, \beta 3, \beta 4, \beta 5$ — row vectors of slope coefficient of regressors

ε_{it} Is Stochastic error term of firm i at time t

u_{it} : error term of firm i at time t

4. Data Analysis and Discussion

Descriptive Statistics

Descriptive statistics are presented in Table 2, showing the mean, maximum, minimum, and standard deviation of the dependent, independent, and control variables. Dividend per Share Has 9.128 mean value and ranged from 0.00 to 55.00 with 14.074 standard Deviation. The mean value of Dividend Pay-out Ratio is 0.470 with 0.630 standard deviation. Dividend Yield ranged from 0.000 to 0.333 and has 0.059 mean value. The value of mean for firm size is 9.882 with the minimum value at 9.075 and the maximum value at 11.049. Leverage has 0.292 mean value with 0.198 deviation. Market Price per Share ranged from 0.255 to 3.653 with 0.745 standard deviation and has 2.011 as mean value. The results indicate the range and distribution of the variables among the 27 Food, Beverage, and Tobacco companies listed in the Colombo Stock Exchange for the period from 2017 to 2021.

Table 2. Descriptive Statistics

Variables	DPS	DPR	DY	FL	FS	MPS
Mean	9.128148	0.470109	0.052419	0.291660	9.882361	2.010718
Maximum	55.00000	2.362205	0.332597	0.763153	11.04991	3.653213
Minimum	0.000000	0.000000	0.000000	0.001773	9.074771	0.255273
Std. Dev	14.07420	0.629969	0.058997	0.198029	0.457511	0.745018
Observations	135	135	135	135	135	135

Unit root Analysis

Unit root analysis is conducted to test the stationarity of the variables. The results in Table 3 indicate that all variables used in the study are stationary at the zero level.

Table 3. Unit root Analysis

Variables	Zero level		Conclusion
	t statistics	Probabilities	
DPS	-5.447421	0.0000	DPS is stationery at zero level
DPR	-9.803153	0.0000	DPR is stationery at zero level
DY	-4.677667	0.0002	DY is stationery at zero level
FS	-4.006138	0.0019	FS is stationery at zero level
FL	-5.457206	0.0000	FL is stationery at zero level
MPS	-5.820370	0.0000	MPS is stationery at zero level

Test for Variance Inflation Factor

The test for variance inflation factor is conducted to detect multicollinearity among the explanatory variables. The results in Table 4 show that all variables have variance inflation factors less than 10 and greater than 0.1, indicating no multicollinearity issues.

Table 4. Variance Inflation Factor (VIF)

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
C	0.943608	478.8589	NA
DPS	1.07E-05	1.520742	1.068098
DPR	0.005182	1.616950	1.035821
DY	0.577579	1.818053	1.012660
FS	0.009868	490.1234	1.040481
FL	0.053529	3.368195	1.057395

Correlation Analysis

Correlation analysis is performed to examine the relationship between dividend policy and shareholders' wealth. The results in Table 5 show the coefficient correlations between dividend per share, dividend pay-out ratio, dividend yield, and market price per share. The findings indicate the nature and significance of the relationships between these variables. The coefficient correlation between dividend pay-out ratio and market price per share is 0.206 significant at 0.05 level, which indicates that there is significant positive relationship between dividend pay-out ratio and shareholders' wealth of Food, Beverage and Tobacco companies in Sri Lanka. Dividend yield has significant negative relationship with shareholders' wealth of Food, Beverage and Tobacco companies in Sri Lanka at 0.05 level. Firm size has positive significant relationship with shareholders' wealth at 0.01 level while firm leverage has insignificant relationship with shareholders' wealth of Food, Beverage and Tobacco companies in Sri Lanka.

Table 5. Correlation Analysis

Correlation Probability	DPS	DPR	DY	FS	FL	MPS
DPS	1.000000 -----					
DPR	0.126182 0.1448	1.000000 -----				
DY	-0.015048 0.8625	0.017053 0.8444	1.000000 -----			
FS	0.112852 0.1925	0.130230 0.1322	0.080721 0.3520	1.000000 -----		
FL	0.196744 0.0222	-0.034247 0.6933	0.073702 0.3956	0.097462 0.2608	1.000000 -----	
MPS	0.666595 0.0000	0.206344 0.0163	-0.188629 0.0285	0.271993 0.0014	0.048387 0.5773	1.000000 -----

Panel data Regression Analysis

Panel data regression analysis is employed to determine the relationship between dividend policy and shareholders' wealth. Pooled OLS, fixed effect, and random effect models are utilized. Results of panel data is presented in Table 6.

Breusch and Pagan Lagrange Multiplier Test and Hausman Specification Test are employed to select the appropriate model. As per the results of these test , the fixed effect model is suitable to test the hypothesis of this study. The findings indicate that dividend per share significantly impacts on shareholders' wealth of Food, Beverage, and Tobacco companies listed in the Colombo Stock Exchange at a 5% significant level (0.007015, P value < 0.05). According to the signalling theory if Dividend per share increases it will reveal the company's future prospectus. Therefore investors want to invest in that company's shares. As a results that company's share prices increases thus share holders' wealth will be maximized. Therefore, hypothesis H₁ is supported, suggesting that there is a significant positive relationship between dividend per share and shareholders' wealth. This finding is in line with Priyan and Nyabakora (2022), David et al., (2022), Yogendrarajah et al. (2022).

As per to the results of fixed effect regression , dividend pay-out ratio doesn't cause any impact in the shareholders' wealth .Due to the financial crisis in Sri Lanka the probability of companies to provide dividend in net income is less. It is reflected by the mean value of Company's dividend pay-out ratio which equals 0.47 and Standard deviation which is 0.629. It shows that most of the companies are unable to pay the dividend at satisfactory level. Furthermore due to the current tax policy of Sri Lanka, companies' net income after tax may be less. The above mentioned points may be the causes for the inability of the dividend pay-out ratio to cause any impact on the shareholders' wealth. However, dividend pay-out ratio is not significantly related to market price per share, failing to support hypothesis H₂. Finding of this study is consistent in related to the findings of Yogendrarajah et al., (2022) and Kengatharan and Ford (2021).

Dividend yield has negative impact on shareholders' wealth(-1.225318, P- Value < 0.01). For this, changes of the interest rate that currently exist may be the main reason. For example during Covid pandemic situation, companies may face difficulties in gathering sources of financing. So if the companies pay more dividend to their shareholders, mostly they will have to depend on the long term loans for their sources of financing. As a result the companies need to pay higher interest, which will decrease the shareholders' wealth by reducing the earning per share. This finding is validated with Yogendrarajah et al., (2022) and Anasar et al.,(2015).

Table 6. Panel data Regression Analysis

Variables	Pooled OLS	Fixed Effect	Random Effect
C	-1.517505 (0.1207)	-8.521322 (0.0000)	-5.083321 (0.0007)
Dividend Per Share	0.034069 (0.0000)	0.007015 (0.0456)	0.013450 (0.0000)
Dividend Pay-out Ratio	0.116227 (0.1088)	0.009345 (0.7123)	0.009884 (0.6947)
Dividend Yield	-2.419286 (0.0018)	-1.225318 (0.0092)	-1.733175 (0.0001)
Firm Size	0.341875 (0.0008)	1.075222 (0.0000)	0.719085 (0.0000)
Leverage	-0.305535 (0.1890)	-0.335619 (0.1404)	-0.167270 (0.4126)
F- Statistics	30.11785 (0.000000)	116.3488 (0.000000)	11.82207 (0.000000)
R- Squared	0.538609	0.972236	0.314232
Redundant fixed Effect Test / Chow Test (Pooled OLS Vs Fixed Effect)		379.417327 (0.0000)	
Breusch and Pagan Lagrange Multiplier Test (Pooled OLS Vs Random Effect)			197.0346 (0.0000)
Hausman Test (Fixed Effect Vs Random Effect)		17.877583 (0.0031)	

5. Conclusion

In conclusion, this study has examined the impact of dividend policy on shareholders' wealth of Food, Beverage, and Tobacco companies listed in the Colombo Stock Exchange. The findings suggest that dividend per share and firm size have a positive impact on shareholders' wealth, while dividend yield has negative impact. Dividend pay-out ratio and financial leverage do not have any impact on shareholders' wealth. These findings contribute to the understanding of dividend policy and its impact on shareholders' wealth, providing insights for management, policymakers, and shareholders. This study recommends that, companies establish consistent dividend policies to enhance share prices thereby increasing the shareholders' wealth. Additionally, businesses should provide the necessary disclosures about their dividend policies to inform investors' investment choices. Future studies could consider expanding the sample size, including various sectors, and extending the time period to further enhance the empirical findings.

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