

# Effect of Dividend Policy on Stock Price in LQ45 Companies

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## Effect of Dividend Policy on Stock Price in LQ45 Companies

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### Abstract:

The purpose of this study is to analyze effect of dividend policy on stock price in LQ45 companies. This research uses a causal research type with a quantitative approach. The population in this study are LQ45 companies listed on the Indonesia Stock Exchange for the 2017-2021 period as many as 64 companies. Based on the selection of criteria that meet the requirements to be selected as many as 30 companies as a sample. The method of data analysis in this study used simple linear regression analysis. The results of the study show that dividend policy has positive and significant effect on stock price.

**Keywords:** Dividend Policy, Stock Price, Indonesia Stock Exchange

### INTRODUCTION

In the current era of globalization, economic development in Indonesia is growing more rapidly and competition is getting tougher. This is indicated by the number of companies in Indonesia that demand companies to maximize their business results in order to be able to compete strongly in the capital market business, so that the company has a goal to increase and maximize company value and prosper the shareholders. Shareholders will tend to maximize the value of the company which is reflected in its share price and force managers to act in their interests through the supervision they do.

The capital market is an activity that trades securities in the form of shares and bonds which is carried out on an exchange where investors meet. The capital market in Indonesia is the Indonesia Stock Exchange. Currently, the Indonesia Stock Exchange has 34 types of stock indices. Stock index means a statistical measure of changes in price movements of a group of stocks selected based on certain criteria and methodologies that are evaluated periodically. The LQ45 index is one of several types of stock price indexes on the Indonesia Stock Exchange.

LQ45 is a combination of companies whose shares have a high level of liquidity, which means the shares are easy to trade, making LQ45 company shares attractive to investors. Shares are one of the securities traded in the capital market that are ownership which is a sign of a person's or business entity's capital participation in a company (Hermuningsih, 2012:78). According to Hidayat (2010:97), shares are a sign of participation or ownership of a person or institution in a company. The company's shares included in the LQ45 index describe that the company's shares have met certain criteria set by the Indonesia Stock Exchange.

According to Darmadji and Fakhruddin (2012:102) stock prices are prices that occur on the stock exchange at a certain time. Stock prices can change up or down in a matter of time so quickly. It can change in minutes or even in seconds. This is possible because it depends on the demand and supply between the stock buyers and the stock sellers. If the stock price of a company is low, it will harm the company, but on the other hand, if the share price of a company is high, it will generate profits for the company. Deden (2011) states that stock prices are determined by market forces, in the sense that they depend on supply and demand (shares are liquid). The amount of demand and supply will reflect market forces.

Shareholders are referred to as shareholders. Stocks will earn dividends. Dividend is a distribution of company profits that will be paid or distributed by the company to shareholders based on the number of shares owned. A company that has a profit every year will think whether from the profit it earns will be given all or part or all of it is held for reinvestment. The size of the dividend to be distributed by the company is determined by the different dividend policies of each company.

Dividend policy is part of the company's spending decisions, especially with regard to the company's internal spending (Sudana, 2011). According to Riyanto (2011), the notion of dividend policy is a policy concerned with determining the distribution of income between users of income to be paid to shareholders as dividends or for use in the company, which means the income must be invested in the company. According to Sartono (2011), dividend policy is a decision whether what is obtained by the company will be distributed to shareholders as dividends or will be retained in the form of retained earnings to finance investment in the future.

The importance of deciding dividend policy by a company in giving dividends to shareholders is because the dividend distribution can increase investors' interest in purchasing company shares, so it is necessary to analyze the factors that can affect dividend policy and how these factors affect the company's share price. By knowing how the factors of dividend policy and their effect on stock prices, it can help companies determine how they should determine dividend policy so that the company's goals to increase company value and optimize shareholder prosperity and welfare are achieved through increasing stock market prices.

The purpose of this study is to analyze effect of dividend policy on stock price in LQ45 companies.

## **LITERATURE REVIEW**

### **Dividend Policy**

Dividend policy is a decision whether the profits earned by the company at the end of the year will be distributed to shareholders in dividends or retained to increase capital to finance investments in the future (Sudana, 2011). In essence, dividend policy is the determination of the amount of profit earned by the company which will be paid in the form of dividends to investors and how much profit is retained for the company's internal spending.

Dividend policy is a policy regarding dividend distribution by company management regarding the amount of dividends to be paid and the amount of retained earnings for future investment needs (Riyanto, 2011). If the company prefers to distribute profits as larger dividends, the retained earnings will be smaller, there by reducing the company's internal sources of funds.

There are three theories related to dividend policy that will explain how the size of the dividend payout ratio affects. The three theories are as follows (Sartono, 2011):

1. Dividend Irrelevance Theory

According to the dividend irrelevance theory, dividend policy does not affect the market price of the company's shares or the value of the company. The theory of irrelevance of dividends reveals that a company's value is determined solely by its profits and business risks, not because of the dividends given. In a world without taxes, and without taking into account transaction costs and in perfect market conditions, dividend policy will not have any effect on the market price of a company's stock.

#### 2. Bird in the Hand Theory

Based on the bird in the hand theory, dividend policy is a view that states that investors will prefer to reinvest dividends in the form of shares in other companies. In bird in the hand theory, shareholders view that dividends are more certain than capital gains. This is because the level of certainty of dividends is higher so that investors tend to buy more shares in the company. If the dividend distributed is higher, it will attract investors to reinvest in the company.

#### 3. Tax Preference Theory

The theory of tax preference suggests that the point is not to like the distribution of dividends in cash, because cash dividends will be taxed more heavily than stock dividends. According to this theory, if the tax imposed on dividends is high and with the possibility of delaying the tax on capital gains, it will have a negative impact on companies paying high dividends, therefore investors will turn away from expecting high dividend payments.

Factors affecting dividend policy In addition to considering the effect of dividends on stock prices, there are other factors that management needs to consider in determining dividend policy (Riyanto, 2011):

#### 1. Funds Needed by the Company

If in the future the company plans to invest which of course requires large amounts of funds, the company can set it aside from retained earnings. If the more budget needed by the company, the greater the portion of retained earnings so that the dividends to be distributed will be smaller.

#### 2. Liquidity

The company is only able to pay dividends if the company's liquidity level is sufficient. The higher the level of liquidity, the greater the cash dividends that the company can pay to shareholders, and vice versa.

#### 3. The Company's Ability to Borrow

One source of company funds is derived from loans. It is possible for the company to pay large dividends, because the company has the opportunity or ability to obtain funds from loans to meet the funding needs of the company. This means that the company's financial leverage is still low, and the company is still trusted by creditors. The more the company's ability to borrow, the greater the dividends distributed to investors.

#### 4. Value of Dividend Information

Based on several research results, it is found that the market price of the company's stock will increase when the company announces an increase in dividend payments, and the stock market price will decrease when the company announces a decrease in dividend payments. An increase in dividend payments indicates that the company's financial performance is good, whereas when the dividend decreases, it signals that the company's financial condition is not in a good condition.

#### 5. Company Control

If the company pays large dividends, the company is likely to obtain funds by selling shares back to finance investment opportunities that are considered profitable. Under

these conditions, the control of shareholders will be reduced if they do not buy back new shares issued by the company. Whereas shareholders may prefer if the company pays low dividends and uses retained earnings to finance company investments.

#### 6. Restrictions Stipulated in the Loan Agreement with the Creditor

When the company gets a loan from the creditor, a loan agreement will arise accompanied by certain requirements. One of the requirements is the limitation of dividend distribution which cannot exceed a certain agreed amount. This is done to protect the interests of creditors.

#### 7. Inflation

The higher the inflation rate, the lower the purchase price of foreign currency. This indicates that the company needs to provide a larger budget to finance operations and investments in the future. Thus, if inflation increases, the dividends to be distributed will decrease and vice versa.

### **Stock Price**

The share price is the money spent to obtain proof of participation or ownership of a company. In the secondary market or in daily stock trading activities, stock price fluctuate either in the form of increases or decreases (Darmadji and Fakhruddin, 2012). The formation of stock price occurs because of the demand and supply of these shares. This supply and demand occurs because of many factors, both factors that are specific to the stock such as the performance of the company and the industry in which the company operates, as well as macro factors such as the country's economic conditions, social and political conditions, as well as rumors that develop.

Stock price fluctuations are determined by the company's ability to earn profits. If the profits obtained for the company are relatively high, it is very possible that the dividends paid are relatively high, will have a positive effect on the stock price on the exchange, and investors will be interested in buying them (Deden, 2011). As a result, the demand for these shares increases, in the end the share price also increases. A share has a price value.

### **RESEARCH METHODS**

This research uses a causal research type with a quantitative approach. Causal research according to Pandiangan (2018) is a type of research where there is a causal relationship between the independent variable (the variable that influences) and the dependent (the variable that is influenced). Quantitative research method is a research method based on the philosophy of positivism, used to examine certain populations or samples, data collection using research instruments, data analysis is quantitative/statistical, with the aim of testing predetermined hypotheses (Asyraini et al., 2022; Octiva et al., 2021).

Population is a generalization area consisting of objects or subjects that have certain qualities and characteristics determined by the researcher to be studied and then drawn conclusions (Octiva et al., 2018; Pandia et al., 2018; Pandiangan et al., 2021). The population in this study are LQ45 companies listed on the Indonesia Stock Exchange for the 2017-2021 period as many as 64 companies. The sample is part of the number and characteristics possessed by the population (Octiva, 2018; Pandiangan et al., 2018; Pandiangan et al., 2022). Based on the selection of criteria that meet the requirements to be selected as many as 30 companies as a sample.

The data collection technique used in this research is the documentation study data collection technique. Documentation study data collection technique is a method used to obtain data and information in the form of books, archives, documents, written

numbers or pictures in the form of a report that can assist in research (Pandiangan, 2015).

The method of data analysis in this study used simple linear regression analysis. Simple linear regression analysis is based on a functional or causal relationship of one independent variable with one dependent variable (Pandiangan, 2022; Tobing et al., 2018).

## **RESULT**

### **Indonesia Stock Exchange**

The Indonesia Stock Exchange is a party that organizes and provides a system as well as a means to bring together offers of buying and selling securities of other parties with the aim of trading securities between them.

The Indonesia Stock Exchange is the result of the merger of the Jakarta Stock Exchange and the Surabaya Stock Exchange. For the sake of operational effectiveness and transactions, the Government decided to merge the Jakarta Stock Exchange as the stock market with the Surabaya Stock Exchange as the bond and derivatives market to become the Indonesia Stock Exchange. The resulting stock exchange began operating on December 1, 2007.

### **Composite Stock Price Index**

The Composite Stock Price Index is one of the stock market indexes used by the Indonesia Stock Exchange. The Composite Stock Price Index was first introduced on April 1, 1983 as an indicator of stock price movements on the Jakarta Stock Exchange. This index covers the price movements of all common and preferred shares listed on the Indonesia Stock Exchange. The base day for calculating the Jakarta Stock Exchange is August 10, 1982. On that date, the index was set at a base value of 100 and the number of listed shares at that time was 13 shares.

The highest intraday position ever achieved by the Composite Stock Price Index was 6,996.93 points recorded on March 1, 2022. The highest closing position ever reached was 6,928.32 points on March 4, 2022.

### **LQ45 Index**

The LQ45 index is a stock market index on the Indonesia Stock Exchange which consists of 45 companies that meet certain criteria, namely:

1. Included in the top 60 companies with the highest market capitalization in the last 12 months.
2. Be included in the top 60 companies with the highest transaction value in the regular market in the last 12 months.
3. Have been listed on the Indonesia Stock Exchange for at least 3 months.
4. Have a high financial condition, growth prospect, and transaction value.
5. Experienced an increase in the free float weight to 100% which was previously only 60% in the assessment portion.

The LQ45 index is calculated every six months by the Research Division of the Indonesia Stock Exchange.

The LQ45 Index was created as an effort to complement the Composite Stock Price Index in particular to provide an objective and reliable tool for financial analysts, investment managers, investors, and capital market observers in monitoring the price movements of stocks that are actively traded on the Indonesia Stock Exchange.

## Simple Linear Regression Analysis Results

**Table 1. Simple Linear Regression Analysis Results**  
Coefficients<sup>a</sup>

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-1453.138	2086.488		-.697	.487
	Dividend Policy	.683	.278	.169	2.456	.015

a. Dependent Variable: Stock Price

Source: Data Processing Results (2021)

The results of the study show that dividend policy has positive and significant effect on stock price. This shows that an increase in dividend policy will be followed by an increase in stock price, otherwise a decrease in dividend policy will cause stock price to decrease. This study shows that the ability of a company to increase dividend will increase the company's stock price. Dividend are related to the amount of dividend distributed to profit after tax. One of the considerations of investors in deciding to buy a stock is the distribution of dividend. With the distribution of dividend, investors can assess the future prospects of the company. From this it can be seen that dividends are a signal for investors to invest in shares.

### CONCLUSION AND SUGGESTION

The results of the study show that dividend policy has positive and significant effect on stock price.

Based on the results of the research that the author has done, the suggestions that the writer can give are as follows:

- 1.As a consideration for investors before making investment decisions and can make profitable investment plans.
- 2.As a reference material and it is hoped that in the next research to increase the number of independent variables because dividend policy is not the only factor that affects stock price.

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