Signaling Theory in Action: How Dividends Affect Shareholder Investment Decisions in Nigerian Deposit Money Banks

Abstract

The study examined how dividends influence shareholder investment decisions in Nigerian listed deposit money banks, thereby testing the applicability of Signaling Theory in this context. Investment decision was measured using the amount of equity shareholding in the bank. *Ex-post facto* research design was applied on the population of all the thirteen (13) listed deposit money banks in Nigeria. The study employed purposive sampling to select ten (10) deposit money banks. Secondary data were sourced from the annual report and accounts of the selected listed banks for ten (10) years from 2013 to 2022. The study utilized Pooled least square regression technique with the aid of Eviews statistical software to test the null hypothesis. The finding showed that dividends significantly increased the amount of equity shareholding among listed deposit money banks in Nigeria (p-value = 0.0000). In conclusion, higher dividends not only signals a bank's current financial health but also enhances investor confidence in its future prospects, leading to greater equity shareholding. Therefore, we recommend that managers of deposit money banks in Nigeria should establish and consistently adhere to transparent dividend policies, providing clear criteria for distribution and maintaining a reliable track record of payouts to build investor confidence.

Keywords: Dividends, Shareholder Investment Decisions, Equity Share Holding, Signaling Theory

1.0 Introduction

Investors worldwide operate in a complex financial environment where making sound investment decisions is paramount. The ability to discern the financial health and performance of companies is a critical aspect of this process [1]. Ratio analysis, which is an integral part of financial analysis, plays a central role in this endeavour because it involves evaluating various financial metrics and using them to get clues on a company's strengths, weaknesses, and overall potential [2,29,30]. By evaluating various financial ratios such as dividend per share, investors can effectively manage risk and tailor their investment choices to align with their specific objectives and risk tolerance. Investors rely on financial accounting information such as dividend payout to inform their investment decisions, among other applications [2]. While shareholder investment decisions is not solely driven by the analysis of dividend ratios [3, 4], it undoubtedly stands as one of the fundamental sources of economic data that influences investment considerations [5].

As per the postulations of signaling theory, the disclosure of accounting information leads to increased awareness in the capital markets, subsequently reducing risks for investors [6, 7]. The stock market serves as a platform for interested parties, including both local and foreign investors, to allocate their funds with the primary objective of generating profits and expanding their wealth. Within the stock market, investors can utilize various financial instruments to effectively manage their liquidity while assessing associated risks [3]. As outlined by Farj, Jais, and Abu [3], the stock market fulfills two pivotal roles. Firstly, it

establishes a vital connection between companies in need of capital for launching new ventures and investors willing to allocate funds to support these enterprises. Secondly, it offers a regulated marketplace for the buying and selling of securities, with prices determined by the forces of supply and demand, taking into account macroeconomic factors like interest rates and inflation. Nigerian Deposit Money Banks, like their counterparts globally, aim to attract and retain investors by consistently paying attractive dividends.

Ideally, a well-structured and transparent dividend policy reflects the bank's financial health and growth prospects, thereby enhancing investor confidence and fostering a robust investment climate [8]. However, a perusal of the annual reports of few listed deposit money banks in Nigeria shows that up to five deposit money banks (Eco bank, Sterling bank, Union bank, Unity bank and Wema bank) have very inconsistent dividend policies and also paid no dividend for some years. Thus, dividend policies in Nigeria often lack consistency, influenced by fluctuating economic conditions, regulatory changes, and internal management decisions. This inconsistency in dividend payouts creates uncertainty among investors regarding the true financial health and future prospects of these banks. Additionally, external economic factors such as inflation and exchange rate volatility further complicate the predictability of dividends, making it challenging for investors to rely on DPS as a stable indicator for their investment decisions.

Consequently, investors, facing uncertainty and inconsistency in dividend payouts, may exhibit reduced confidence in the Nigerian banking sector, potentially leading to lower investment levels. This reluctance can stymie the growth and stability of the banks, as they rely on steady investment inflows to fuel their operations and expansion. Furthermore, the perceived unpredictability in dividend policies can deter both local and foreign investors. This situation underlines the need for a more consistent approach to dividend policies which could serve as a signal that enhances investor confidence in terms of equity shareholding. While prior studies have extensively investigated the impact of various financial metrics and accounting information on investment decisions in different contexts, there is a notable gap in research specifically addressing the influence of dividends on shareholder investment decisions within Nigerian listed deposit money banks. This study aims to fill this gap by testing the applicability of Signaling Theory in this particular setting, providing hints into the role dividends play in shaping investment behaviours in the Nigerian banking sector.

2.0 Review of Related Literature

2.1 Conceptual Review

2.1.1 Dividends and Dividend Per Share

A dividend is a distribution of a portion of a company's earnings to its shareholders, typically in the form of cash payments, additional shares of stock, or other property [9]. Dividends are usually declared by the company's board of directors and are distributed at regular intervals, such as quarterly or annually. They represent a reward to shareholders for their investment in the company and can be an indicator of the company's financial health and profitability [10]. The amount and frequency of dividends can vary based on the company's earnings, financial policies, and overall economic conditions. Dividend per share (DPS) is the portion of a company's earnings distributed to each outstanding share of common stock, representing the return on investment for shareholders in the form of dividends. Dividend per share (DPS) signifies the total dividends disbursed by a company for each outstanding ordinary share, according to Amahalu, Abiahu, Obi, and Nweze [11]. This metric encompasses the entirety of dividends distributed by a company, encompassing interim dividends, and divides

this sum by the count of ordinary shares currently in circulation. The calculation of a company's DPS generally hinges on the dividends paid during the latest quarter, and this figure is concurrently employed in computing the dividend yield.

Dividend per share represents the cumulative dividend payouts for each ordinary share issued by a company. It encompasses the entire annual dividend distribution, which includes interim dividends but excludes special dividends. This figure is then divided by the total number of outstanding ordinary shares that have been issued by the company. DPS is a fundamental accounting ratio employed to assess the total dividend amount declared for each share of common stock issued. It's important to emphasize that when calculating DPS, the focus is solely on the common stock that has been issued by the company. This ratio serves as a valuable indicator for investors and analysts in evaluating a company's dividend distribution in relation to its common shares [12].

2.1.2 Shareholder Investment Decision

Shareholder investment decisions refer to the choices made by investors to allocate their financial resources in various assets or projects with the expectation of achieving specific financial goals or returns [13]. Shareholders' investment decisions encompass the careful selection of where to allocate their current funds or other valuable resources within a specific company, driven by the anticipation of future gains. As articulated by Muhammadi [14], these investment decisions revolve around the effective allocation of capital, particularly with regard to the commitment of funds to long-term assets. These choices hold significant sway over the firm's overall value and size, exerting a profound influence on aspects such as growth, profitability, and risk, as highlighted by Zayol, Agaregh, and Eneji [8]. Consequently, investment decisions transcend mere financial commitments; they serve as pivotal determinants of a firm's trajectory and prosperity.

Due to the critical nature of investment decisions, a great deal of prudence is essential [15]. These decisions involve substantial, limited, and hard-earned resources, carry an irreversible aspect, and bear risks with enduring consequences that no investor wishes to grapple with in the event of unfavorable outcomes [16]. Notably, investments in the stock market loom as a primary area of interest for individuals seeking to make the most of their financial assets [13].

2.2 Development of Hypotheses Based on Signalling Theory

Signaling theory, initially propounded by Michael Spence in 1973, originates from the field of economics and deals with how individuals convey their private information to others. Spence introduced the concept to address the issue of information asymmetry in the job market, where job seekers signal their abilities to potential employers through educational credentials [7].

The core postulation of signaling theory is that parties with more information (the insiders) send signals to less informed parties (the outsiders) to convey important information [17]. In the context of financial markets, companies use signals like dividend payouts to communicate their financial health and future prospects to investors [18]. According to the theory, higher dividend payouts signal strong earnings and stable financial conditions, thereby attracting more investment. Conversely, a reduction in dividends might signal potential financial difficulties or lower future earnings, potentially deterring investment [19].

In line with this signaling theory, Nigerian banks, like other firms, use dividends as a tool to signal their financial robustness and future growth potential to current and prospective

investors. Given the prevalent information asymmetry in financial markets, especially in developing economies like Nigeria, consistent and attractive dividend payouts can enhance investor confidence and guide investment decisions. However, the inconsistency in dividend policies observed in Nigerian Deposit Money Banks disrupt this signaling process, leading to investor uncertainty and potentially reduced investment inflows. We therefore hypothesise that: dividends will have a significant positive effect on shareholder investment decision. In other words, the higher dividends will increase the equity shareholding among listed deposit money banks in Nigeria.

2.3 Evidence from Prior Literature

Olayinka [2] conducted a study to investigate the impact of financial statement analysis on investment decisions within Nestlé Nigeria Plc. The study utilized data from Nestlé Nigeria Plc's annual reports, employing descriptive statistical analytical tools for data presentation and interpretation. The study concluded that financial statement analysis is a valuable tool for informed decision-making.

Alqam, Ali, and Hamshari [20] investigated the effect of financial ratio analysis on investment decisions in Jordan. The sample size comprised 55 respondents from firms listed on the Amman Stock Exchange (ASE). The study employed simple linear regressions to test its hypotheses and found that financial ratios were indeed utilized by data users when making investment and lending decisions. The results showed that investors predominantly focused on profitability and market ratios when making their investment decisions.

Shodiya, Sanyaolu, Ojenike, and Ogunmefun [21] investigated the effect of dividend per share on investment decisions in food and beverage companies listed in Nigeria. To achieve this, seven listed food and beverage companies were selected. The research adopted an ex post facto research design, utilizing purposeful and stratified sampling techniques to select seven out of the fifteen companies in the food and beverage subsector. Data for the study were extracted from the annual reports and accounts of the sampled companies from 2008 to 2017. The results obtained from the regression analysis reveal that dividend per share has a non-significant positive effect on investment decisions.

Bamidele, Ibrahim, and Omole [22] explored the influence of financial reporting quality on investment decision-making by Deposit Money Banks, with a reference to Zenith Bank Plc in Nigeria. The study used audited annual reports of Zenith Bank Plc from 2009 to 2016. A combination of descriptive analysis and Ordinary Least Square Regression was used for data analysis, facilitated by E-View 9.0 statistical software. The findings revealed that higher financial reporting quality positively influenced investment decisions made by Deposit Money Banks in Nigeria.

Amaraihu and Onodi [23] studied the effect of financial information on investor confidence in listed manufacturing firms in Nigeria. The study employed an ex-post-facto research design and utilized simple regression analysis for data analysis. The research found that dividend coverage had a positive impact on investor confidence.

Aderemi, David, Adetiloye and Eriabie [6] investigated the impact of accounting information in financial statements on shareholders' investment decision-making among 1,000 staff members in universities located in Ogun and Lagos states of Nigeria. The research employed a survey research design and utilized structured questionnaires to gather perceptions from shareholders regarding the importance of financial statements for investment decision-making. The study conducted empirical tests using ANOVA and the Likelihood Ratio Test.

The results indicated that shareholders possessed the necessary skills to analyze International Financial Reporting Standards (IFRS) financial statements and relied on the information disclosed in these statements for their investment decisions. The study recommended the use of ratio analysis, trend analysis, and common size analysis in addition to accounting figures to obtain deeper hints into financial information.

Zayol, Agaregh, and Eneji [8] conducted an empirical investigation into the influence of financial accounting information on the investment decisions of bank shareholders in Nigeria. Data for the study were collected from published annual reports of five selected banks in Nigeria spanning from 2009 to 2015. Correlation matrix and regression analysis were utilized to establish the relationships between variables. The results unveiled a positive relationship, highlighting the significant impact of dividend per share on the investment decisions of bank shareholders in Nigeria.

Thuhoye [24] examined the relationship between accounting information and investment decisions, with a focus on TANESCO Morogoro as a case study. The study adopted a descriptive survey research design and targeted a population of 50 staff members of TANESCO Morogoro. The primary method of data collection involved the use of questionnaires, while secondary methods included library research for relevant materials. The collected data were analyzed using SPSS software. The findings indicated a significant relationship between accounting information and investment decisions, with all selected areas significantly relying on accounting information for investment decision-making.

Nwaobia, Kwarbai, Olajumoke and Ajibade [25] investigated the influence of financial reporting quality on investors' decisions using ten selected manufacturing companies listed on the Nigerian Stock Exchange. The study covered a five-year period from 2010 to 2014 and employed various analytical methods, including correlation matrix, Vector Auto Regressive Estimation, and Pooled OLS model. The findings revealed a positive association between earnings per share and investors' decisions.

Farj, Jais, and Abu [3] explored the significance of accounting information contained in corporate annual reports published in the Libyan Stock Market from the perspective of investors as primary users of these reports. The research adopted a descriptive survey research design and gathered information from all shareholders using a set of questionnaires. The study utilized proxies such as return on assets ratio, return on equity ratio, and net cash flow and employed T-statistic as the statistical tool for data analysis. The findings suggested that corporate financial reports are considered valuable, although they are not the primary source of information influencing investors' decisions. Libyan investors tend to rely more on advice obtained from brokers when making their decisions rather than thoroughly examining corporate annual reports.

Irandoost, Hassanzadeh, and Salteh [26] assessed the effect of dividend policy on investment decisions. The statistical community of the present research includes firms admitted to the Tehran Stock Exchange, of which 65 firms were selected after applying the considered criteria. The research covered a period of three years from 2007 to 2012, and correlation analysis method and multiple regressions were used to analyze the data and test the hypotheses. The research results indicate that dividend policy does not have a significant effect on investment decisions.

Osuala, Ugwumba, and Osuji [4] explored the effect of ratio analysis on shareholders' investment decisions in selected firms in Nigeria. The study applied regression analysis and concluded that regularity of dividend payment and market price of shares are vital to shareholders' investment decisions.

3.0 Methodology

In order to determine examine how dividends influence shareholder investment decisions in Nigerian listed deposit money banks, thereby testing the applicability of Signaling Theory in this context, the study adopted *ex-post facto* research design. *Ex-post facto* research design is considered appropriate for this study since the researcher seeks to examine the nexus between variables that co-occurred in the past [27, 28]. The population for the study covered all the thirteen listed deposit money banks in Nigeria (see **Table 1**).

Table 1 Study Population
1. Access Bank Nigeria Plc.
2. Ecobank Transnational Incorporated Bank Nigeria Plc.
3. Fidelity Bank Nigeria Plc.
4. First Bank Nigeria
5. First City Monument Bank Nigeria
6. Guaranty Trust Bank
7. Stanbic IBTC
8. Sterling Bank
9. Union Bank
10. United Bank for Africa Plc.
11. Unity Bank
12. Wema Bank Plc.
13. Zenith Bank Nigeria Plc.

Source: Nigerian Exchange Group (2022)

The study employed purposive sampling to select ten deposit money banks. The reason for the use of this sampling was because it allows researchers to specifically select participants or cases that are most relevant to the research questions or objectives. The criterion for being selected is complete availability of financial reports and audited accounts data during the specified period. Table 2 provides the names of the banks included in the sample.

Table 2 Study Sample Size
1. Access Bank Nigeria Plc.
2. Ecobank Transnational Incorporated Bank Nigeria Plc.
3. Fidelity Bank Nigeria Plc.
4. Guaranty Trust Bank
5. Sterling Bank
6. Union Bank
7. United Bank for Africa Plc.
8. Unity Bank
9. Wema Bank Plc.
10. Zenith Bank Nigeria Plc.

Source: Researcher's Compilation (2023)

Secondary data was used in the study. Data relating to dividend and investment decision were sourced from the annual report and accounts of the selected listed banks for ten (10) years from 2013 to 2022. For the purpose of this study, the operational measurement of the variables is given as follows in **Table.3**.

Table.3 Measurement of Variables

Variable	**Type**	**Acronym**	**Measurement**	**Source**

1. Investment Decision	Dependent	IVD	Amount of equity shareholding in the year end	[21]
2. Dividend	Independent	DPS	Total amount of dividend paid in a period	[9]

Source: Researcher's Compilation (2023)

The model tested in the study is specified below:

$IVD_{it} = \alpha_0 + \beta_1 DIVS_{it} + \mu_{it}$ _____eqn (i)

Where,

IVD_{it} = Investment Decision for bank i in period t.

$DIVS_{it}$ = Dividends paid by bank i in period t

μ_{it} = white noise for firm i in period t.

α_0 = constant.

β_1 = coefficient of the predictor

The descriptive statistics of the data in this study was carried out with the aid of mean and standard deviation. More so, the study utilized Pooled Least Square regression technique with the aid of Eviews statistical software to test the null hypothesis. The use of Pooled OLS analytical method is justified in the study since it provides a framework for analysing the effect of independent variable on a dependent variable using data that have both time series and cross-sectional dimensions. By pooling the data, the sample size increases, which can improve the precision of the estimates and lead to more robust statistical inference.

4.0 Result and Discussion

Table 4. shows the descriptive analysis of the secondary data collected for the purpose of the study.

Table 4. Descriptive Analysis

	N	*Minimum*	*Maximum*	*Mean*	*Std. Deviation*
INV	100	-278,855,888	6,822,517,000	379,753,954.04	716074544.593
DIVS	100	0	97328000	19194962.07	27367470.420

Source: Analysis Output using Eviews 10 (2024)

As shown in Table 4. above, Investment Decision (IVD) comprises 100 observations. The minimum value recorded is -278,855,888, indicating a significant loss or negative investment in some instances. Conversely, the maximum value reaches 6,822,517,000, reflecting a very high level of equity shareholding by some investors. The mean value, which stands at 379,753,954.04, represents the average amount of equity shareholding across the sample, suggesting that on average, investors hold a substantial amount of equity. However, the standard deviation of 716,074,544.593 points to a high level of variability in the data, indicating that the equity shareholdings vary widely among different investors.

For the Dividend per Share (DIVS), the dataset also includes 100 observations. The minimum value is 0, indicating that some companies did not pay any dividends during the period under study. The maximum dividend per share is 97,328,000, showing that some companies offered very high dividends. The mean dividend per share is 19,194,962.07,

suggesting that, on average, the companies paid a moderate amount of dividends per share. The standard deviation of 27,367,470.420 indicates significant variability in the dividends paid, which implies that the dividend payments were quite inconsistent among the different companies.

4.1 Test of Hypothesis

The study utilized Pooled least square regression technique to test the null hypothesis as shown below in Table 5

Table 5 Test of Hypotheses Using Pooled Least Square Regression

Dependent Variable: IVD
Method: Pooled Least Squares
Date: 06/02/24 Time: 13:10
Sample: 2013 2022
Included observations: 100
Cross-sections included: 1
Total pool (balanced) observations: 100

Variable	Coefficient	Prob.
DIVS	14.10420	0.0000
Adjusted R-squared	0.283330	
F-statistic	40.13895	
Prob(F-statistic)	0.000000	

Source: Analysis Output using Eviews 10 (2024)

Table 5 presents the results of the hypothesis testing using pooled least squares regression, with Investment Decision (IVD) as the dependent variable and Dividend per Share (DIVS) as the intendent variable. The adjusted R-squared value is 0.283330. This statistic measures the proportion of the variance in the dependent variable (IVD) that is explained by the independent variable (DIVS) after adjusting for the number of predictors in the model. An adjusted R-squared value of 0.283330 implies that approximately 28.33% of the variation in investment decisions can be explained by the dividends per share. While this indicates a moderate level of explanatory power, it also suggests that there are other factors influencing investment decisions that are not captured by this model. The F-statistic for the model is 40.13895, with an associated probability (Prob(F-statistic)) of 0.000000. The F-statistic tests the overall significance of the regression model. Given the very low probability value, the F-statistic is highly significant, indicating that the model as a whole is a good fit for the data. This further confirms that dividends per share significantly contribute to explaining the variations in investment decisions among the sampled companies.

As per test of hypothesis, the pooled least squares regression analysis demonstrates a significant positive relationship between dividends per share and investment decisions, as evidenced by the positive coefficient, and highly significant p-value. The coefficient for DIVS is 14.10420, which indicates that for every unit increase in dividend per share, the investment decision proxy (amount of equity shareholding) increases by 14.10420 units. This positive relationship implies that higher dividends per share are associated with higher levels of investment by shareholders. The probability value (Prob.) associated with the DIVS coefficient is 0.0000. This p-value is highly significant, far below the common significance level threshold

of 0.001. The near-zero p-value strongly indicates that the relationship between dividend per share and investment decision is not due to random chance. In other words, the effect of dividends on investment decisions is statistically significant, reinforcing the idea that dividends play a crucial signalling role in influencing shareholders' investment behaviours.

Investors are generally attracted to companies that distribute dividends consistently. A positive correlation between dividend and investment decisions suggests that investors in Nigerian deposit money banks find dividends appealing. This may be attributed to the fact that dividends provide a tangible return on investment, offering investors a steady income stream. Additionally, a consistent dividend payout can be indicative of a company's stable financial position and the management's confidence in its future earnings. This finding is consistent with the study by Amaraihu and Onodi [23]; Alqam, Ali, and Hamshari [20]; and Zayol, Agaregh, and Eneji [8].

5.0 CONCLUSION AND RECOMMENDATIONS

In exploring the dynamics of Signaling Theory within Nigerian deposit money banks, this study focuses on how dividend policies influence shareholder investment decisions, specifically measured by equity shareholding. The findings indicate a significant and positive correlation between dividends and shareholder investment behaviour. This result aligns with the fundamental premise of Signaling Theory, which posits that firms use dividend announcements as a means to convey valuable information about their financial health and future prospects to the market.

Dividends serve as a critical signal to investors regarding a company's profitability and stability. When a bank announces higher dividends or maintains a consistent dividend payout ratio, it signals to shareholders that the bank has generated sufficient earnings to distribute profits. This act not only reflects current financial strength but also suggests confidence in future earnings stability. For Nigerian deposit money banks, a robust dividend policy can enhance investor trust and attract long-term equity investment.

Moreover, dividends are often perceived as tangible rewards for shareholders, providing immediate returns on their investment. This aspect makes dividend-paying stocks particularly appealing to income-oriented investors seeking regular cash flows. As such, a positive relationship between dividends and equity shareholding can be attributed to investors' preference for securities that offer both potential capital appreciation and income stability. Thus, by effectively signaling financial health and commitment to shareholder returns, dividends not only influence current investor behaviour but also contribute to long-term shareholder loyalty and market stability. This finding reinforces the applicability of Signaling Theory in understanding investor responses to dividend policies within the unique context of Nigerian financial institutions. We therefore recommend that managers of deposit money banks in Nigeria should establish and consistently adhere to transparent dividend policies, providing clear criteria for distribution and maintaining a reliable track record of payouts to build investor confidence.

Limitation and Scope for Further Research

One limitation of the study is its reliance on secondary data sourced solely from annual reports and accounts. While these documents provide detailed financial information, they may not capture all factors influencing shareholder investment decisions, such as qualitative aspects of dividend announcements or investor sentiment. Future research could explore the impact of qualitative factors on shareholder investment decisions in Nigerian listed deposit money banks. Qualitative factors could include investor perceptions of management credibility, market

expectations regarding dividend policies, or the effects of macroeconomic conditions on investment decisions. Additionally, comparative studies across different industries or countries could provide hints into how signaling theory applies in various financial contexts.

Disclaimer (Artificial intelligence)

Author(s) hereby declare that generative AI technologies such as Large Language Models, etc have been used during writing or editing of manuscripts. We used DeepAI, accessible at https://deepai.org, as a writing assistant to receive suggestions for improving the clarity of specific paragraphs within the research proposal. By entering the prompt, "Provide suggestions for enhancing the clarity and coherence of the paragraph below," into DeepAI, the generated content offered clues for improving language usage and grammar. This feedback from DeepAI was a beneficial resource, guiding and informing my research and writing process by providing refined language options that seamlessly integrated into our work.

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