

ABSTRACT

This study examines the effects of dividend cuts and omission on the performance of South African firms listed on the Johannesburg Stock Exchange (JSE) over the sample period of 1996 and 2016. The study examines an overlooked area in dividend change studies and is motivated by the conflicting conclusions that exist in finance literature around what dividend reductions signal to the market. The study made use of a total of 94 firms which comprises both the dividend decrease and omission sample as well as the control (peer) firm sample. The study employs the event study methodology using the control firm and the capital asset pricing model (CAPM) to test for the effect of dividend cuts and omissions on the share price. The study also tests for the relationship between dividend cuts and omissions and variables such as the return on assets (ROA), the market to book ratio (M/B) and the capital expenditure (CAPEX). The study finds negative abnormal returns for both control adjusted returns and the CAPM adjusted returns. The market to book ratio results show that there is a decrease in growth prospects for both high and low market to book ratio firms. In terms of the return on asset analysis, dividend decrease sample firms were found have had poor operating performance years prior the dividend cut announcement and continued to experience poor operating performance years after the cut, suggesting that dividend decrease firms were not as profitable and hence the reason to cut dividends. The dividend decrease firms were found to increase capital expenditures even years after the dividend decrease announcement whereas the opposite was found for control firms. The overall results are consistent with international literature where changes in dividends appear to be linked to changes in future growth opportunities.