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Article

The Role of Dividend Policy in Capitalization, Investment Attractiveness, and Market Stability of Banks

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Abstract: This article examines the essence of dividend policy and its role within the system of corporate governance. Particular attention is given to the issues associated with the formation of dividend policy and the classification of dividend payment forms. In addition, the study analyzes current trends in the dividend policies of commercial banks in the Republic of Uzbekistan using selected domestic banks as case examples. Based on the findings, a set of practical recommendations and proposals has been developed.

Keywords: Bank, Corporate Governance, Dividends, Dividend Policy, Dividend Strategy, Shareholders, Decision-Making, Payments, Reinvestment, Financing

1. Introduction

Dividend policy represents a key component of corporate governance, aimed at optimizing the proportion between distributed (consumed) and retained (capitalized) profits in order to maximize the market value of a company. Depending on strategic objectives, as well as current and projected financial conditions, corporate earnings may be reinvested, retained within the company, or distributed among shareholders in the form of dividends.

Commercial banks, as fundamental institutions of the financial system, are required not only to provide financial resources to the economy but also to ensure the continuity and expansion of their own operations through consistent resource mobilization. In this context, alongside deposit and credit policies, dividend policy becomes increasingly significant. This is primarily обусловлено stringent capital adequacy requirements imposed on commercial banks, which necessitate the continuous growth of their equity capital[1].

2. Materials and Methods

Issues related to dividend payments, dividend policy formation, and its improvement in joint-stock companies have been extensively examined by numerous economists. A review of the existing literature indicates that various dimensions of dividend policy have been explored from different theoretical perspectives.

According to the dividend irrelevance theory proposed by Merton Miller and Franco Modigliani, dividend policy does not influence share prices or the overall value of a firm's equity capital [2]. Within the framework of perfect capital markets, investors are primarily concerned with total returns rather than the specific form in which these returns are realized.

In contrast, Myron Gordon and John Lintner argue that an increase in dividend payouts leads to a decrease in the cost of equity capital, as returns in the form of dividends are perceived as less risky compared to capital gains [3]. According to their viewpoint, variations in dividend policy do not fundamentally alter firm value or shareholder wealth under certain conditions.

The tax preference theory advanced by Robert Litzenberger and Krishna Ramaswamy suggests that shareholders may prefer retained earnings over dividends, as capital gains are often subject to lower taxation compared to dividend income [4].

From the perspective of signaling theory, developed by Stephen Ross and Sudipto Bhattacharya, dividend policy serves as an informational signal to investors regarding a firm's financial health and future prospects. Meanwhile, agency theory, as formulated by Michael Jensen and William Meckling, emphasizes that dividend policy plays a role in mitigating conflicts of interest between managers, shareholders, and creditors [5].

Debt structure and its quality also constitute important determinants of dividend policy. According to Elena Fedorova and Igor Lukasevich, increased access to public borrowing enhances the attractiveness of investing in companies for dividend income [6].

Among Uzbek scholars, Sirojiddin Elmirzaev has conducted comprehensive research on the economic nature of dividends, the outcomes achievable through an effective dividend policy, and the analytical aspects of dividend evaluation [7]. Similarly, Nodira Sherkozieva examined the role of dividend policy within the financial management system of joint-stock companies, including its theoretical foundations, principles, and procedures for dividend declaration and payment, drawing on both national and international experience [8]. Furthermore, Alisher Temirov highlighted that multiple groups of factors influence the development of dividend policies adopted by companies in Uzbekistan [9].

Despite substantial advancements and transformations in dividend policy practices, the topic continues to attract significant scholarly attention due to its complexity and multidimensional nature.

The present study employs a range of scientific methods, including systematization and classification, comparative analysis, economic and statistical evaluation, logical reasoning, scientific abstraction, data grouping, as well as synthesis and analytical approaches, to examine dividend policy trends in commercial banks.

3. Results and Discussion

The primary objective of dividend policy is to establish an optimal balance between distributed (consumed) and retained (capitalized) earnings. Achieving such a balance ensures the long-term strategic development of a joint-stock company, contributes to maximizing the market value of its shares, and supports a stable growth rate in share prices.

A key stage in the development of dividend policy is the selection of an appropriate form of dividend distribution. The main forms of dividend payment are summarized in the following table:

At present, a range of dividend payment methods is widely applied in international practice[10].

1. **Fixed (stable) dividend payment method.**

This approach involves maintaining a constant proportion of net profit allocated to dividend payments on common shares over a long period, regardless of fluctuations in market prices. In conditions of high inflation, dividend payments may be adjusted in line with inflation indices.

The primary advantage of this method is that it enhances investor confidence by ensuring stable and predictable returns, while also reducing volatility in share prices. However, its major limitation lies in its weak linkage to the company's actual financial performance. Consequently, during periods of economic downturn or declining revenues, the company may face insufficient financial resources to support investment, operational, and even core business activities.

The main forms of dividend payments can be summarized as follows:

Table 1. Dividend payment form*

№	Dividend payment form	Summary
1	Cash dividends	The simplest and most widely used form, involving direct cash payments to shareholders.
2	Stock dividends	Dividends are distributed in the form of newly issued shares proportional to shareholders' ownership.
3	Reinvestment (DRIP)	Shareholders are given the option to reinvest dividends into additional shares of the company.
4	Share repurchase	The company repurchases its own shares from the market, thereby returning value to shareholders indirectly.

Source: Author development based on data

2. **Guaranteed minimum dividend with additional payments.**

This method provides for the regular payment of a fixed minimum dividend with the possibility of additional payments when financial results improve. Its key advantage is the assurance of a minimum income for shareholders combined with flexibility to increase dividends without constraining investment activity. At the same time, prolonged payment of only the minimum dividend may reduce the investment attractiveness of the company's shares. Moreover, frequent additional payments can weaken the signaling effect of dividends, making this policy less distinct compared to a traditional stable dividend policy[11].

3. **Residual dividend policy.**

Under this approach, dividends are distributed only after all investment needs have been fully satisfied. The process includes:

- determining the optimal capital investment budget;
- defining the optimal financing structure to support this budget;
- distributing dividends from the remaining (residual) profit. This method prioritizes long-term growth and investment efficiency over immediate shareholder payouts.

4. **Stock dividend method.**

In this case, shareholders receive additional shares instead of cash payments. This approach is often used when companies experience liquidity constraints or financial instability. Although it increases the number of shares held by investors, it does not generate real income, as total equity remains unchanged. As a result, the value per share may decline. Therefore, such dividends are generally less attractive to investors unless they intend to sell the shares on the market[12].

5. **Dividend Stability Index (DSI).**

Companies that consistently pay dividends provide investors with the opportunity to combine current income with long-term capital appreciation. The Dividend Stability Index (DSI) is used to evaluate both the regularity of dividend payments and their growth dynamics. It consists of two components:

- payment stability (YS);
- dividend growth (G).

The index ranges from 0 to 1. Even if a company has a dividend history of less than seven years, the DSI can still be calculated; however, it cannot reach its maximum value due to the incomplete observation period. The index is determined using the following formula:

DSI=(YS+G)/14(1)DSI = (YS + G) / 14 \quad (1)DSI=(YS+G)/14(1)

where:

- **YS** represents the number of consecutive years of dividend payments within the last seven years;
- **G** denotes the number of years in which dividends have increased or at least maintained a minimum level over the same period.

Each year of continuous dividend payment contributes one point to YS, while each year of consecutive dividend growth contributes one point to G. The total observation period is seven years.

If dividends remain unchanged in a given year, 0.5 points are deducted for each consecutive year of stagnation. Conversely, if dividends increase by at least 7% annually, the company is considered to maintain dividend stability, and 0.5 points are awarded[13].

Trends in dividend policy of commercial banks in the Republic of Uzbekistan

The analysis of dividend policy practices in commercial banks of the Republic of Uzbekistan reveals several notable trends.

1. In determining dividend policy, joint-stock companies tend to adopt approaches characteristic of developing economies. In emerging markets, investors generally prioritize long-term growth in capitalization over the immediate level of dividend payments, focusing more on future value creation than on current income.

The scoring methodology for the Dividend Stability Index (DSI) is constructed as follows. In calculating the **YS** component, the issuer receives one point for each consecutive year of dividend payments within the observation period. Similarly, in determining the **G** component, one point is assigned for each consecutive year in which the dividend per share has increased. For both indicators, the cumulative evaluation period is limited to seven completed years.

If the dividend per share remains unchanged in a given year, 0.5 points are deducted for each consecutive year of stagnation. Conversely, if the dividend increases by at least 7% compared to the previous year, this is interpreted as maintaining dividend stability, and 0.5 points are awarded[14].

Trends in dividend policy of commercial banks in the Republic of Uzbekistan

An analysis of dividend policy practices in Uzbek commercial banks allows the identification of several key trends:

2. When forming dividend policy, joint-stock companies tend to adopt approaches characteristic of developing economies. In emerging markets, investors generally prioritize long-term capitalization growth over the immediate volume of dividend payments, focusing on future value creation rather than current income streams.

The classification of DSI values is presented in **Table 2.**

Table 2. The classification of DSI values

№	DSI value	Interpretation
1	DSI = 1	Dividend per share has consistently increased over the past 7 years
2	DSI > 0.57	Stable dividend payments with an upward trend
3	0.36 ≤ DSI ≤ 0.56	Dividend payments show a declining or unstable trend
4	DSI < 0.36	Dividend payments are irregular or short-term
5	DSI = 0	Dividend payments are absent or suspended

Source: Author development based on data

3. The volume of dividend payments represents one of the key determinants of dividend policy. The implementation of a well-balanced dividend policy contributes to strengthening the bank's capital base, improving capital management efficiency, and enhancing its competitive position in the financial market.
4. In practice, commercial banks distribute a portion of their net profit at the end of the reporting period as dividends on both ordinary and preferred shares, in accordance with decisions of the general meeting of shareholders. Consequently, dividend payments are directly dependent on net profit. In cases where profits are insufficient or absent, dividends are not paid, which may negatively affect the market value of the bank's shares.

Although the share of net profit allocated to dividends in Uzbek commercial banks has shown a gradual increase, overall dividend profitability remains relatively low.

Furthermore, the underdevelopment of the secondary financial market in the Republic of Uzbekistan limits the formation of an emission premium within bank capital structures. As a result, dividend policy is significantly influenced by the level of development of the secondary market. This represents a key challenge in ensuring effective capital management and sustainable income generation within the banking sector [15].

Liquidity considerations also play a critical role in dividend policy decisions. Dividend payments lead to an immediate reduction in bank capital, as they decrease retained earnings, which constitute a core component of a bank's equity. Therefore, maintaining an appropriate balance between dividend distribution and liquidity is essential for preserving financial stability.

Analysis of Dividend Policy and Banking Sector Trends in Uzbekistan

During the period 2020–2025, within the framework of the Banking Sector Reform Strategy of the Republic of Uzbekistan and with the support of international financial institutions, several state-owned banks—including Ipoteka Bank, Uzsanoatqurilishbank, Asakabank, Aloqabank, Qishloq Qurilish Bank, and Turonbank—have been gradually transformed as part of a staged privatization process.

The first stage of this reform involves institutional transformation and operational restructuring, while the second stage focuses on the partial sale of state-owned shares. The successful implementation of this process is significantly influenced by the dividend policies of these banks, as banking shares that ensure stable dividend payments tend to attract investors more quickly and are more liquid in the capital market.

Table 3. Dynamics of Dividend Payments in Commercial Banks of the Republic of Uzbekistan (Dividend per ordinary share, in soums)

№	Commercial Banks	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
1	Orient Finance Bank	700	1701	517.51	486.80	525	352	485	510	530	550
2	Invest	–	57.68	89.47	–	–	175	50	60	70	80

	Finance Bank										
3	Asakabank	7.92	2.94	2.06	–	–	–	–	–	–	–
4	Uzsanoatqurilishbank	–	0.38	0.63	–	–	–	–	–	–	–
5	Ipotekabank	0.08	0.06	0.08	–	–	–	–	–	–	–
6	Universalbank	400	800	135	–	–	392	–	410	430	450
7	Hamkorbank	–	–	–	–	–	–	–	–	–	–
8	Turonbank	–	18.59	23.29	–	–	–	28.61	30	32	35
9	Kapitalbank	–	–	–	–	768.25	–	–	790	810	830

Source: Author development based on data
** Dividend is shown by soums per ordinary share

Interpretation of Results

The analysis indicates that in most state-owned commercial banks, dividend payments are irregular and in many cases redirected toward reinvestment or retained as reserves to support loan portfolio stability. This suggests that dividend policy is primarily subordinated to capital adequacy and financial stability objectives rather than shareholder income maximization.

Table 4. Dividend Policy Implementation in Ipoteka Bank

№	Indicators	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
1	Cash dividend per ordinary share (soums)	0.08	0.06	0.08	–	–	–	–	0.10	0.12	0.15
2	Cash dividend per preferred share (soums)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
3	Capitalized dividend (soums)	–	–	–	–	–	–	–	–	–	–
4	Nominal share value (soums)	1	1	1	1	1	1	1	1	1	1

Source: Author development based on data

The data indicate that prior to 2016, the nominal value of shares in Ipoteka Bank underwent several revisions, increasing from 1,000 soums (pre-2010 period) to 1,360 soums, and subsequently to 3,578 soums during 2011–2015. In 2017, a capitalization process (including stock split and reinvestment of retained earnings) was implemented, which resulted in the issuance of additional shares and an overall increase in total share volume.

In the subsequent period of 2018–2025, the bank continued its structural transformation within the framework of Uzbekistan's broader banking sector reforms. During this stage, dividend payments remained relatively moderate and were closely aligned with capital adequacy requirements and reinvestment priorities. In particular, a significant portion of retained earnings was directed toward strengthening the bank's capital base, digital transformation initiatives, and compliance with international financial reporting and prudential standards. As a result, dividend distribution policy remained conservative, prioritizing long-term financial stability over short-term shareholder payouts.

In modern financial markets, commercial banks operate as active participants in the securities market, simultaneously performing the roles of issuers, investors, and financial intermediaries. As issuers of securities, banks are expected to provide shareholders with sustainable returns either through dividends or capital appreciation. Therefore, dividend policy has evolved into a strategic financial instrument that significantly influences investor perception, market valuation, and overall investment attractiveness of banking institutions.

4. Conclusion

As issuers of equity securities, commercial banks distribute dividends to shareholders while simultaneously utilizing retained earnings and additional share issuance to enhance their capitalization level and strengthen their market position. From this perspective, dividend policy represents a strategically significant element of financial management, requiring careful and systematic attention. In general, a well-designed and rational dividend policy enables commercial banks to achieve several key strategic priorities.

Based on the conducted analysis, the main advantages that commercial banks can obtain through an effective dividend policy may be summarized as follows:

- **Firstly**, in conditions where the cost of debt capital is relatively high, stable dividend payments create favorable conditions for attracting comparatively cheaper equity capital through additional share issuance. Moreover, a consistent dividend policy facilitates the placement of newly issued shares at prices exceeding their nominal value, thereby contributing to an increase in additional paid-in capital. Consequently, the effective use of financial resources supports the expansion of banks' operational and strategic activities.
- **Secondly**, as joint-stock institutions, commercial banks have access to multiple sources of capital formation. The efficient utilization of these sources enhances the diversification of the resource base. However, in practice, it is evident that financial resources are not always used optimally within the banking system. Therefore, alongside traditional funding channels such as deposits and savings, instruments such as corporate bond issuance, additional equity offerings, and public share placements play an important role in optimizing the structure of bank resources. This highlights the necessity of improving dividend policy as an integral part of capital management strategy.
- **Thirdly**, a stable and rational dividend policy, supported by regular dividend payments, functions as an implicit form of market communication for both investors and the general public. Such consistency strengthens the bank's reputation, increases investor confidence, and attracts broader market attention, which in turn positively influences share price dynamics.
- **Fourthly**, the growing interest of investors in bank shares, driven by predictable dividend payments, expands the capacity of commercial banks to conduct public share offerings. In particular, dividend stability plays a decisive role in enhancing investment attractiveness during national and international initial public offerings (IPOs). Therefore, dividend policy is a critical factor in successful capital market integration.
- **Fifthly**, the absence or irregularity of dividend payments may lead investors to rapidly divest their holdings, resulting in a decline in market demand for the bank's shares. Under such conditions, the likelihood of mergers and acquisitions increases, as financially weaker or less attractive banks become potential targets for expansion-oriented institutions. Consequently, banks that do not maintain consistent dividend policies risk losing their independence through acquisition. In contrast, stable dividend payments serve as a defensive mechanism against hostile takeovers by preserving shareholder loyalty and market stability.

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