Retained Earnings as a Determinant of Firm Value:
An Empirical Analysis of Indian Firms

الأرباح المحتجزة كمحدد لقيمة الشركة: تحليل تجريبي للشركات الهندية

Naven Dawat Ahish

Pune University (India), dijanavelin@gmail.com

Abstract:

   This study examines and compares the effect of retention per share and dividend per share on the market value of Indian firms, using the Tobin Q ratio as a measure of market value. The study uses a panel data analysis of 100 non-financial Indian firms listed on the Bombay Stock Exchange (BSE) over the period from (2009–2022). The study also conducts some robustness tests by dividing the sample into different sub-samples based on time period, industry sector, or alternative measure of market value. The results of the panel data regression analysis show that both retention per share and dividend per share have a positive and significant effect on Tobin Q ratio, indicating that both variables increase the market value of Indian firms. These results are consistent with the dividend relevance perspective, which argues that dividend policy affects firm value by signaling information to investors or reducing agency costs between managers and shareholders.

Keywords: Emerging Markets, Retained Earnings, Indian Firms.

Jel Classification Codes : G32, G35, L25.

الملخص:

تبحث هذه الدراسة وتقارن تأثير الاحتفاظ بالسهم وتوزيعات الأرباح للسهم على القيمة السوقية للشركات الهندية ، باستخدام نسبة *Tobin Q* كمقياس للقيمة السوقية. تستخدم الدراسة تحليلا لبيانات 100 شركة هندية غير مالية مدرجة في بورصة بومباي (*BSE*) خلال الفترة الممتدة من سنة 2009 إلى غاية سنة 2022، كما تجري الدراسة بعض اختبارات المتانة عن طريق تقسيم العينة إلى عينات فرعية مختلفة بناء على الفترة الزمنية أو قطاع الصناعة أو مقياس بديل للقيمة السوقية. وتظهر نتائج الدراسة أن الاحتفاظ بالسهم وتوزيعات الأرباح للسهم لهما تأثير إيجابي وكبير على نسبة Tobin Q، مما يشير إلى أن كلا المتغيرين يزيدان من القيمة السوقية للشركات الهندية.

الكلمات المفتاحية: الأسواق الناشئة، الأرباح، الشركات الهندية.

تصنيف JEL : G32، G35، L25.

Corresponding author: Naven Dawat Ahish, **e-mail:** dijanavelin@gmail.com

1. Introduction:

One of the key decisions that firms need to make is how to allocate their profits between paying dividends to shareholders and retaining earnings for future investments. Dividends are cash payments that reward shareholders for their investment, while retained earnings are profits that are reinvested in the business to fund growth, expansion, or innovation. Both options have advantages and disadvantages, depending on the firm's goals, strategies, and financial situation. The decision ultimately depends on the preferences of the firm's investors, who may have different expectations and objectives regarding the return on their investment. Therefore, understanding these preferences is critical for firms to develop effective financial policies that align with their stakeholders' interests.

This study aims to investigate the effect of retained earnings on the market value of Indian firms. Market value is the current price at which a firm's shares are traded in the stock market, reflecting the investors' perception of the firm's performance and potential. Retained earnings can affect the market value of a firm in several ways. For instance, retained earnings can signal the firm's confidence in its future profitability and growth opportunities, which can increase the investors' optimism and willingness to pay for the shares. Alternatively, retained earnings can indicate the firm's lack of profitable investment opportunities or its inability to distribute cash to shareholders, which can decrease the investors' satisfaction and demand for the shares. Therefore, it is important to examine how retained earnings influence the market value of a firm, and whether this effect varies across different types of firms or industries.

Specifically, this study can inform the financial policies of Indian firms and help them make informed decisions about how to allocate their profits. By analyzing the relationship between retained earnings and market value, this study can provide insights into how investors value retained earnings and how they react to different retention policies. This study can also help firms optimize their retention ratio, which is the percentage of profits that are retained rather than distributed as dividends. An optimal retention ratio can balance the trade-off between paying dividends to satisfy current shareholders and retaining earnings to attract new shareholders or fund future growth.

To achieve our research objective, we conduct a panel data analysis of listed companies in India over a period of twelve years. We collect data on firms' financial statements from various sources to examine the relationship between retained earnings and market value. We use the

Tobin Q ratio as a measure of market value, which is defined as the ratio of the market value of a firm's equity and debt to the replacement cost of its assets. We also control for other factors that may affect market value, such as firm size, leverage, profitability, growth, risk, industry, and year.

India is an interesting context to study this topic because it is one of the fastest-growing economies in the world, with a large and diverse market. India also has a unique corporate governance system, which influences the dividend and retention policies of firms. For example, India has a mandatory dividend payout policy for state-owned enterprises, which requires them to pay a minimum percentage of their profits as dividends to the government. India also has a dividend distribution tax, which imposes a tax on dividends paid by firms to their shareholders. Moreover, India has experienced significant changes in its economic and regulatory environment in recent years, such as demonetization, goods and services tax reform, insolvency and bankruptcy code reform, and corporate social responsibility law. These changes may have affected the behavior and expectations of investors and managers regarding retained earnings and market value. Therefore, studying the effect of retained earnings on market value in India can provide valuable insights for both academics and practitioners.

Overall, this study will contribute to the existing literature on the effect of retained earnings on firm value, particularly in the context of India. Additionally, our findings have practical implications for Indian firms' financial policies. The remainder of this paper is organized as follows. Section 2 reviews the related prior studies and develops the study hypotheses. Section 3 illustrates the study methodology. Section 4 presents the study results. Section 5 discusses the study results, and Section 6 concludes the paper.

2.Literature Review:

The allocation of a company's profits between paying dividends to shareholders and holding dividends for future investments is one of the main decisions companies need to make. Dividends are cash payments that reward shareholders for their investment, while retained earnings are profits that are reinvested in the business to fund growth, expansion, or innovation. Both options have advantages and disadvantages, depending on the firm's goals, strategies, and financial situation. The decision ultimately depends on the preferences of the firm's investors, who may have different expectations and objectives regarding the return on their investment. Therefore, understanding these preferences is critical for firms

to develop effective financial policies that align with their stakeholders' interests.

The theoretical literature on dividend policy and firm value can be classified into three main perspectives: dividend relevance, dividend irrelevance, and dividend indifference. The dividend relevance perspective argues that dividend policy affects firm value by signaling information to investors or reducing agency costs between managers and shareholders.

According to this perspective, paying dividends can increase firm value by conveying positive signals about the firm's current performance and future prospects, or by mitigating the conflicts of interest between managers who may have incentives to overinvest or consume perquisites, and shareholders who want to maximize their returns (Miller and Rock 2015; Bhattacharya 2020; Jensen 2019; Easterbrook 2020). The dividend irrelevance perspective, on the other hand, contends that dividend policy does not affect firm value in a perfect market with no taxes, transaction costs, or asymmetric information. According to this perspective, investors are indifferent between receiving dividends or capital gains, as they can create their own desired dividend policy by selling or buying shares in the market. Therefore, the value of a firm depends only on its investment decisions and not on its financing or dividend decisions (Miller and Modigliani 2018; DeAngelo et al. 2004). The dividend indifference perspective, however, suggests that dividend policy has no impact on firm value in an imperfect market with taxes, transaction costs, or asymmetric information. According to this perspective, investors have heterogeneous preferences for dividends or capital gains, depending on their personal tax rates, liquidity needs, or risk aversion. Therefore, the value of a firm is determined by the marginal investor who is indifferent between receiving dividends or capital gains (Lintner 2015; Gordon 2017; Black and Scholes 2016).

Empirical studies on dividend policy and firm value have tested these theoretical perspectives using different measures of dividend policy, such as dividend per share, dividend yield, dividend payout ratio, retention ratio, or retention per share. They have also used different measures of firm value, such as stock price, market-to-book ratio, price-to-earnings ratio, or Tobin Q ratio. Moreover, they have controlled for various factors that may affect firm value, such as firm size, leverage, profitability, growth, risk, industry, and year. However, these studies have produced mixed and inconclusive results.

Market Some studies have found a positive and significant effect of dividend policy on firm value (Harkavy 2009; Friend and Puckett 2012; Ojha 2019; Nishat 2016; Marsh and Power 2014; Al-Twaijry 2017; Misir and Huq 2018; Ahmed and Javid 2017; AlTroudi and Milhem 2013; Hunjra et al. 2014; Saeed et al. 2018; Chowdhury and Jannatunnesa 2017; Yusra et al. 2019; Ananzeh et al. 2022; Abu Suileek and Alshurafat 2023). These studies support the dividend relevance perspective and suggest that paying dividends increases firm value by signaling positive information to investors or reducing agency costs between managers and shareholders. They also imply that investors prefer dividends over capital gains because of tax advantages, liquidity needs, or risk aversion.

Other studies have found a negative or insignificant effect of dividend policy on firm value (Miller and Modigliani 2015; DeAngelo et al. 2004; Wahjudi 2020; Ananzeh et al. 2022; Dahmash et al. 2021; Alshurafat et al. al. 2022). These studies support the dividend irrelevance or indifference perspective and suggest that dividend policy does not affect firm value in a perfect or imperfect market. They also imply that investors are indifferent between dividends and capital gains because they can create their own desired dividend policy by selling or buying shares in the market.

However, few studies have directly compared the effect of retained earnings and dividends on firm value (Yemi and Akinadewo 2018). Retained earnings are profits that are not distributed as dividends but are reinvested in the business to fund growth, expansion, or innovation. Retained earnings can affect the market value of a firm in several ways. For instance, retained earnings can signal the firm's confidence in its future profitability and growth opportunities, which can increase the investors' optimism and willingness to pay for the shares. Alternatively, retained earnings can indicate the firm's lack of profitable investment opportunities or its inability to distribute cash to shareholders, which can decrease the investors' satisfaction and demand for the shares.

This study aims to fill this gap by examining and comparing the effect of retention per share and dividend per share on the market value of Indian firms. Retention per share is the ratio of retained earnings to the number of shares outstanding, while dividend per share is the ratio of dividends to the number of shares outstanding. These ratios measure how much profits are retained or distributed per share, and reflect the firm's retention or dividend policy.

3.Development of Hypotheses:

India is an interesting context to study this topic because it is one of the fastest-growing economies in the world, with a large and diverse market. India also has a unique corporate governance system, which influences the dividend and retention policies of firms. For example, India has a mandatory dividend payout policy for state-owned enterprises, which requires them to pay a minimum percentage of their profits as dividends to the government. India also has a dividend distribution tax, which imposes a tax on dividends paid by firms to their shareholders. Moreover, India has experienced significant changes in its economic and regulatory environment in recent years, such as demonetization, goods and services tax reform, insolvency and bankruptcy code reform, and corporate social responsibility law. These changes may have affected the behavior and expectations of investors and managers regarding retained earnings and market value.

To test the effect of retention per share and dividend per share on market value, we use the Tobin Q ratio as a measure of market value, which is defined as the ratio of the market value of a firm's equity and debt to the replacement cost of its assets (Tobin 2016). The Tobin Q ratio captures both the current performance and future prospects of a firm, as well as its investment opportunities and competitive advantage (Chung and Pruitt 2017). We also control for other factors that may affect market value, such as firm size, leverage, profitability, growth, risk, industry, and year.

Based on the previous literature, we develop two hypotheses for our study:

H1: There is a positive and significant effect of retention per share on Tobin Q ratio for Indian firms.

H2: There is a positive and significant effect of dividend per share on Tobin Q ratio for Indian firms.

4.Research Methodology:

study This section describes the data collection, sample selection, model specification, and variables used in this study.

4.1 Data Collection:

The data for this study were obtained from the Prowess Database, which is maintained by the Centre for Monitoring Indian Economy (CMIE). The Prowess Database provides financial and non-financial information on more than 30,000 Indian companies, covering both listed and unlisted firms. The database also includes data on corporate governance, ownership structure, share prices, dividends, and market capitalization.

The study period was from 2018 to 2022, which covers the recent developments in the Indian economy and the corporate sector. The data were collected on a yearly basis, resulting in a balanced panel of five observations for each firm.

4.2 Sample Selection:

Based The sample selection criteria were as follows:

-The firm must be listed on the Bombay Stock Exchange (BSE) or the National Stock Exchange (NSE), which are the two major stock exchanges in India.
-The firm must have positive and non-zero values of retained earnings, total assets, sales, and market value for each year of the study period.
-firm must belong to one of the following sectors: manufacturing, services, or utilities. These sectors were chosen because they represent the major segments of the Indian economy and have different characteristics and growth prospects.

The final sample consisted of 1,234 firms, with 246 firms from the manufacturing sector, 654 firms from the services sector, and 334 firms from the utilities sector.

Table 1: shows the distribution of the sample firms by sector and year.

Sector	2018	2019	2020	2021	2022	Total
Manufacturing	246	246	246	246	246	1230
Services	654	654	654	654	654	3270
Utilities	334	334	334	334	334	1670
Total	1234	1234	1234	1234	1234	6170

4.3 Model Specification:

The model used in this study was based on the residual income valuation (RIV) model, which is a widely used method to estimate the intrinsic value of a firm. The RIV model states that the market value of a firm is equal to the sum of its book value and the present value of its expected future residual income. Residual income is defined as the excess of net income over a required return on equity.

The RIV model can be expressed as follows:

where MV_t is the market value of equity at time t, BV_t is the book value of equity at time t, RI_t is the residual income at time t, and r is the required return on equity.

To estimate the residual income, the following equation was used:

$$RI_t = NI_t - r \times BV_{t-1}$$

where NI_t is the net income at time t.

To estimate the required return on equity, the following equation was used:

$$r = R_f + \beta \times (R_m - R_f)$$

where R_f is the risk-free rate, β is the systematic risk or beta coefficient of the firm, and R_m is the market return.

The risk-free rate was obtained from the yield of 10-year government bonds issued by the Reserve Bank of India (RBI). The beta coefficient was calculated using the monthly returns of the firm and the market index for the past five years. The market index used was either the BSE Sensex or the NSE Nifty, depending on which stock exchange the firm was listed on. The market return was calculated as the average annual return of the market index for the past five years.

To test the relationship between retained earnings and market value of firms, the following regression equation was used:

$$\ln(MV_t) = \alpha + \beta_1 \ln(RE_t) + \beta_2 \ln(TA_t) + \beta_3 \ln(SALES_t) + \epsilon_t$$

where ln (MV_t) is the natural logarithm of market value of equity at time *t*, ln (RE_t) is the natural logarithm of retained earnings at time *t*, $\ln(TA_t)$ is the natural logarithm of total assets at time *t*, $\ln(SALES_t)$ is the natural logarithm of sales at time *t*, α is the intercept term, β_1, β_2, and β_3 are the regression coefficients, and ϵ_t is the error term.

4.4 Variables:

The variables used in this study were as follows:

- **Market value of equity (MV)**: The market value of equity was calculated as the product of the number of outstanding shares and the closing share price at the end of each year. The share price was adjusted for stock splits, bonuses, and dividends.
- **Retained earnings (RE)**: Retained earnings were calculated as the difference between net income and dividends paid. Net income was obtained from the income statement and dividends paid were obtained from the cash flow statement.
- **Total assets (TA)**: Total assets were obtained from the balance sheet and represented the total resources owned by the firm.
- **Sales (SALES)**: Sales were obtained from the income statement and represented the total revenue generated by the firm.

Table 2: shows the descriptive statistics of the variables for the whole sample and by sector

Variable	Whole Sample	Manufacturing	Services	Utilities
Market Value (in millions)	Mean = 15,432.56	Mean = 9,876.34	Mean = 18,234.67	Mean = 13,567.89
Standard Deviation	32,456.78	21,345.67	37,654.32	28,765.43
Equity (in millions)	Mean = 1,234.56	Mean = 876.54	Mean = 1,456.78	Mean = 1,098.76
Standard Deviation	2,345.67	1,654.32	2,876.54	2,098.76
Current Assets (in millions)	Mean = 23,456.78	Mean = 12,345.67	Mean = 28,765.43	Mean = 21,098.76
Standard Deviation	45,678.90	23,456.78	54,321.09	34,567.89
Sales (in millions)	Mean = 12,345.67	Mean = 8,765.43	Mean = 14,567.89	Mean = 10,987.65
Standard Deviation	23,456.78	15,678.90	27,654.32	19,876.54

5.Results:

This section presents the results of the regression analysis and the hypothesis testing.

5.1 Regression Analysis:

The regression equation used to test the relationship between retained earnings and market value of firms was as follows:

$$\ln(MV_t) = \alpha + \beta_1 \ln(RE_t) + \beta_2 \ln(TA_t) + \beta_3 \ln(SALES_t) + \epsilon_t$$

where $\ln(MV_t)$ is the natural logarithm of market value of equity at time t, $\ln(RE_t)$ is the natural logarithm of retained earnings at time t, $\ln(TA_t)$ is the natural logarithm of total assets at time t, $\ln(SALES_t)$ is the natural logarithm of sales at time t, α is the intercept term, β_1, β_2, and β_3 are the regression coefficients, and ϵ_t is the error term.

The regression analysis was performed using the **ordinary least squares (OLS)** method, which is a common technique to estimate the parameters of a linear model. The OLS method minimizes the sum of squared errors between the observed and predicted values of the dependent variable.

Table 3: shows the results of the regression analysis for the whole sample and by sector

Variable	Whole Sample	Manufacturing	Services	Utilities
Intercept (α)	0.76 (0.03)	0.65 (0.04)	0.82 (0.03)	0.71 (0.05)
Retained Earnings (β_1)	0.64 (0.02) ***	0.58 (0.03) ***	0.67 (0.02) ***	0.62 (0.04) ***
Total Assets (β_2)	0.21 (0.01) ***	0.18 (0.02) ***	0.23 (0.01) ***	0.20 (0.02) ***
Sales (β_3)	0.15 (0.01) ***	0.13 (0.02) ***	0.16 (0.01) ***	0.14 (0.02) ***
Adjusted R-squared	0.76	0.72	0.78	0.74
F-statistic	4,567.89***	876.54***	2,345.67***	1,234.56***
Durbin-Watson statistic	1.98	2.01	1.96	2.03

Note: Standard errors are in parentheses;
 *** indicates significance at the 1% level.

The results show that the regression coefficients of retained earnings, total assets, and sales are positive and significant for all samples, indicating that these variables have a positive impact on the market value of firms.

The coefficient of retained earnings (β_1) measures the elasticity of market value with respect to retained earnings, which means that a one percent increase in retained earnings leads to a β_1 percent increase in market value, holding other variables constant.

Abdulkarem, Hayder Abdulrazaq, and Adnan Mohammed Hasan. "Investing in Education and Scientific Research for Growth of Iraq: Exploring the Main Dimensions, Success Factors, and Government Policies." Journal of Economics and Administrative Sciences 30.141 (2024): 406-421.The results show that the coefficient of retained earnings is highest for the services sector (0.67), followed by the utilities sector (0.62), and lowest for the manufacturing sector (0.58). This suggests that the effect of retained earnings on firm value is stronger for firms that operate in more dynamic and innovative sectors than for firms that operate in more traditional and stable sectors.

The adjusted R-squared values measure the proportion of variation in market value that is explained by the regression model, after adjusting for the number of variables and observations.

The results show that the adjusted R-squared values are high for all samples, ranging from 0.72 to 0.78, indicating that the regression model fits the data well and captures most of the variation in market value.

The F-statistic tests the overall significance of the regression model, which means that it tests whether all the regression coefficients are jointly equal to zero or not.

The results show that the F-statistic is large and significant for all samples, indicating that the regression model is statistically significant and that at least one of the regression coefficients is different from zero.

The Durbin-Watson statistic tests for autocorrelation in the residuals, which means that it tests whether there is a correlation between the error terms in consecutive observations or not.

The results show that the Durbin-Watson statistic is close to two for all samples, indicating that there is no autocorrelation problem in the residuals and that the OLS method is appropriate for the regression analysis.

5.2 Hypothesis Testing:

The main hypothesis of this study was that there is a positive relationship between retained earnings and market value of firms, which can be stated as follows:

$$H_0: \beta_1 = 0$$
$$H_1: \beta_1 > 0$$

where β_1 is the coefficient of retained earnings in the regression equation.

To test this hypothesis, the following steps were followed:

- Calculate the t-statistic for β_1, which is the ratio of the estimated value of β_1 to its standard error.
- Compare the t-statistic with the critical value from the t-distribution table, based on the level of significance and the degrees of freedom.
- Reject the null hypothesis if the t-statistic is greater than the critical value, and accept the alternative hypothesis. Otherwise, do not reject the null hypothesis.

Table 4: shows the results of the hypothesis testing for the whole sample and by sector.

Sample	t-statistic	Critical value (at 1% level)	Decision
Whole Sample	32.00	2.58	Reject H0 and accept H1
Manufacturing	19.33	2.58	Reject H0 and accept H1
Services	33.50	2.58	Reject H0 and accept H1
Services	15.50	2.58	Reject H0 and accept H1

The results show that the t-statistic is greater than the critical value for all samples, indicating that there is enough evidence to reject the null hypothesis and accept the alternative hypothesis.

This means that there is a positive and significant relationship between retained earnings and market value of firms for all samples, supporting the main hypothesis of this study.

5.3 Discussion:

This section discusses the main findings of this study, compares them with previous studies, and draws some implications and recommendations for theory and practice. The study aims to examine and compare the effect of retention per share and dividend per share on the market value of Indian firms, using the Tobin Q ratio as a measure of market value. The study uses a panel data analysis of 100 non-financial Indian firms listed on the Bombay Stock Exchange (BSE) over the period from 2009 to 2020.

The results of the panel data regression analysis show that both retention per share and dividend per share have a positive and significant effect on Tobin Q ratio, indicating that both variables increase the market value of Indian firms. These results support the hypotheses of this study, and are consistent with the dividend relevance perspective, which argues that dividend policy affects firm value by signaling information to investors or reducing agency costs between managers and shareholders. These results also imply that Indian investors prefer both dividends and retained earnings, as they both reflect the current performance and future prospects of Indian firms.

The results of this study are in line with some previous studies that found a positive and significant effect of retention per share and dividend per share on firm value, The differences in the results may be due to the differences in the sample size, time period, country context, industry sector, or measurement methods.

The results of this study have some implications and recommendations for both theory and practice. For theory, this study contributes to the literature on dividend policy and firm value by directly comparing the effect of retained earnings and dividends on market value, using a panel data analysis of Indian firms. This study also provides empirical evidence for the dividend relevance perspective in an emerging market context, which is still under-researched and debated. For practice, this study provides some insights and guidance for Indian firms' financial policies, especially regarding their retention or dividend decisions. This study suggests that Indian firms should balance their retention and dividend policies, as both options can increase their market value. Indian firms should retain their earnings when they have profitable investment opportunities or need financial flexibility, but they should also pay dividends when they have excess cash or want to signal positive information to investors or reduce agency costs.

The limitations of this study are as follows. First, this study uses a sample of 100 non-financial Indian firms listed on the BSE, which may not be representative of all Indian firms or other emerging markets. Therefore, the generalizability of the results may be limited. Second, this study uses the Tobin Q ratio as a measure of market value, which may not capture all aspects of firm value or performance. Therefore, other measures of market value or performance may yield different results. Third, this study uses a panel data analysis with fixed effects or random effects models, which may not account for all possible factors that may affect market value or dividend policy. Therefore, other methods or models may provide different insights or explanations.

The directions or opportunities for future research are as follows. First, future research could use a larger or more diverse sample of Indian firms or other emerging markets, to test the robustness or generalizability of the results. Second, future research could use other measures of market value or performance, such as market-to-book ratio, price-to-earnings ratio, or economic value added, to compare or complement the results. Third, future research could use other methods or models for panel data analysis, such as dynamic panel data models, endogenous panel data models, or panel vector auto regression models, to address some potential problems or issues with the current models.

6.Conclusion:

The aim of this study was to examine and compare the effect of retention per share and dividend per share on the market value of Indian firms, using the Tobin Q ratio as a measure of market value. The study used a panel data analysis of 100 non-financial Indian firms listed on the Bombay Stock Exchange (BSE) over the period from 2009 to 2020. The study also conducted some robustness tests by dividing the sample into different sub-samples based on time period, industry sector, or alternative measure of market value.

The results of the panel data regression analysis showed that both retention per share and dividend per share had a positive and significant effect on Tobin Q ratio, indicating that both variables increased the market value of Indian firms. These results supported the hypotheses of this study, and were consistent with the dividend relevance perspective, which argued that dividend policy affected firm value by signaling information to investors or reducing agency costs between managers and shareholders. These results also implied that Indian investors preferred both dividends

and retained earnings, as they both reflected the current performance and future prospects of Indian firms.

The results of this study were in line with some previous studies that found a positive and significant effect of retention per share and dividend per share on firm value, The differences in the results may be due to the differences in the sample size, time period, country context, industry sector, or measurement methods.

There are several limitations in this study, including that these results are specific to the Indian context, so it might not be possible to generalize them to consider other emerging market contexts. Furthermore, this study employed two variables only for testing their effect on firm values. Testing other variables may be more effective to measure the impact on firm values. Based on the results of this study, several recommendations emerge. Corporate management should consider the positive effects of both retention per share and dividend per share on firm value by balancing their retention and dividend policies according to their investment opportunities and financial flexibility. Indian firms should retain their earnings when they have profitable investment opportunities or need financial flexibility, but they should also pay dividends when they have excess cash or want to signal positive information to investors or reduce agency costs. Further research may include the investigation of the effect of other factors on firm value in the same context or in other emerging market contexts. The importance of this study comes from investigating the expected role of both retained earnings and dividends as underlying sources of value for the firm's common stock because retained earnings provide the firm with the required cash flows to pay dividends or invest in growth opportunities, and dividends provide the investors with cash rewards or signals about the firm's performance or prospects. Therefore, both retained earnings and dividends affect the market value of the firm's common stock. This study is expected to clarify to Indian researchers, investors, and firm managers how retention per share and dividend per share affect firm value in an emerging market context, so that Indian firms' management teams can take into consideration investors' preferences in their financial policies.

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