DIVIDEND POLICY OF DALMIA CEMENTS (BHARAT) LIMITED, DALMIAPURAM

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Abstract

Financial Management is that managerial activity which is concerned with the planning and controlling of the firm's financial resources. Although it may be difficult to separate the finance functions from production, marketing and other functions yet the financial functions can be easily identified. A dividend is a distribution of divisible profits of a company among the members according to the number of shares held by them. A dividend is declared in the annual general meeting on the basis of the recommendations of the board of directors. This study has been undertaken to analyze the dividend policy of Dalmia Cement (Bharat) Ltd. The general argument is that dividends declared by the company are only nominal and that the shareholder would be better off if the company retained it for further investments.

INTRODUCTION

Dividend decisions is a major decision in financial management and one of the objectives of financial management is to maximize the wealth of the shareholders the firm would be well advised to use. The net profits for paying dividends if it maximizes the wealth of the owners.

A dividend is a distribution of divisible profits of a company among the members according to the number of shares held by them. A dividend is declared in the annual general meeting on the basis of the recommendations of the board of directors. Though the shareholders, may declare dividend smaller than that recommended by the board they cannot declare a larger dividend or any dividend when the board has recommended none.

The board of directors may declare from time to time an interim dividend based on the profits earned by the company and the final dividend will be paid in addition to the interim dividend.

From the year 1997-1998 dividend income has been completely exempted from tax while the capital gains are taxable. Thus Indian shareholders may prefer dividend to capital gains. The companies on the other hand will have to pay tax at 10 percent on the dividend distributed to shareholders.

The usual practice is to pay dividends in cash and other option is distribution of bonus shares.

Most companies pay dividends in cash. Sometimes cash dividend may be supplemented by a bonus issue. A company should have enough cash in its bank account. When the company follows a stable policy it should prepare a cash budget to indicate the necessary funds, which would be needed to meet the regular dividend payments of the company. It is relatively difficult to make cash planning.
In anticipation of dividend needs when an unstable policy is followed.

An issue of bonus shares represents a proportionate distribution of shares in addition to cash dividend to the existing shareholders. This has the effect of increasing the number of outstanding shares. The declaration of bonus will increase the paid-up share capital of the company and reduce its reserves and surplus.

**Following factors Influence the Dividend Policy, They are**

Expectations of the investors, reduction of Uncertainty, indication of strength, legal requirements, contractual requirements, internal constraints, owner’s considerations, capital market considerations, inflation.

The financial manager has to decide whether the firm should distribute all the profits, or retain them, or distribute a portion and retain the balance. The dividend policy should be determined in terms of its impact on the shareholders value. Dalmia Cement (Bharat) Ltd has a history of stable payout of cash dividend along with regular bonus issues.

This study has been undertaken to analyze the dividend policy of Dalmia Cement (Bharat) Ltd.

**OBJECTIVES OF THE STUDY**
1) To study the factors influencing the dividend policy of companies.
2) To analyze the dividend policy of Dalmia Cement (Bharat) Limited.
3) To study the relationship between dividends and market price and earnings and market price of shares.

The study has been based on the data relating to a five-year period that is from the financial year 2003-2004 to 2007-2008.

The study relies on secondary data for the purpose and in certain cases the relevant data have been collected from the financial statements of the company.

**DIVIDEND PAYOUT RATIO**

The payment ratio is the percentage share of the net earnings distributed to the shareholders as dividends. The payout ratio of the firm should be determined with reference to two basic objectives namely,

Maximizing the wealth of the owners and providing sufficient funds to finance growth.

These objectives are not mutually exclusive but interrelated. Generally firms that have substantial investment opportunities and consequently considerable funding needs tend to keep their payout ratio rather low to facilitate growth.

**Formula**

\[
Payout\ Ratio = \frac{Dividend\ Per\ share}{Earnings\ per\ share} \]

\[
Dividend\ per\ share = \frac{Dividend\ paid\ to\ equity\ share\ holders}{Number\ of\ ordinary\ share\ outstanding}
\]

\[
Earnings\ per\ share = \frac{Net\ profit\ available\ to\ equity\ share\ holders}{Number\ of\ ordinary\ shares\ outstanding}.
\]
Table 1. Payout Ratio

<table>
<thead>
<tr>
<th>Year</th>
<th>Earnings per share (Rs.)</th>
<th>Dividend Per Share (Rs.)</th>
<th>Payout Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-2004</td>
<td>4.27</td>
<td>5</td>
<td>111.10</td>
</tr>
<tr>
<td>2004-2005</td>
<td>4.91</td>
<td>5</td>
<td>101.83</td>
</tr>
<tr>
<td>2005-2006</td>
<td>11.78</td>
<td>2</td>
<td>16.98</td>
</tr>
<tr>
<td>2006-2007</td>
<td>29.18</td>
<td>3</td>
<td>10.28</td>
</tr>
<tr>
<td>2007-2008</td>
<td>42.87</td>
<td>4</td>
<td>9.33</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Dalmia Cement (Bharat) Limited.

There has been a gradual increase in payment of dividends except the year 2005-2006, when dividend has decreased from 5 in 2004-2005 to 2 in 2005-2006. After that the dividend remains constant in the years 2006-2007 and 2007-2008 as a rate of 4.

DIVIDEND YIELD AND EARNINGS YIELD

The dividend yield is the dividend per share dividend by the market value per share and the earnings yield is the earnings per share divided by the market value per share. The dividend yield and earnings yield evaluate the shareholders return in relation to the market value of the share. The earnings yield is also called the earnings price ratio.

**Formula:**

- **Dividend Yield** = Dividend per share/Market Value per share
- **Earnings Yield** = Earnings per share/Market value per share

Table 2. Dividend Yield And Earning Yield

<table>
<thead>
<tr>
<th>Year</th>
<th>Earnings per share (Rs.)</th>
<th>Dividend Per Share (Rs.)</th>
<th>Market price (Rs)</th>
<th>Dividend Yield (%)</th>
<th>Earnings Yield (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-2004</td>
<td>4.27</td>
<td>5</td>
<td>288</td>
<td>1.74</td>
<td>1.48</td>
</tr>
<tr>
<td>2004-2005</td>
<td>4.91</td>
<td>5</td>
<td>392</td>
<td>1.27</td>
<td>1.25</td>
</tr>
<tr>
<td>2005-2006</td>
<td>11.78</td>
<td>2</td>
<td>265</td>
<td>0.75</td>
<td>4.45</td>
</tr>
<tr>
<td>2006-2007</td>
<td>29.18</td>
<td>3</td>
<td>361</td>
<td>0.83</td>
<td>8.08</td>
</tr>
<tr>
<td>2007-2008</td>
<td>42.87</td>
<td>4</td>
<td>284</td>
<td>1.41</td>
<td>15.09</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Dalmia Cement (Bharat) Limited.

There has been a fluctuating trend in the earnings per share and consequently the market price also has the same fluctuating trend. The market price shows an increasing trend except in the year 2004-2005. While the earnings yield has been growing at a steady rate, the dividend yield has shown a marked decrease in 2007-2008 due to the natural calamities that affects profits in the year 2007-2008.
PRICE EARNINGS RATIO

The price earnings ratio is the reciprocal of the earnings yield ratio. This ratio is widely used by the security analysis to value the firm’s performance as expected by the investors. It indicates investor’s judgment or appraisal about the firm’s performance. Management is also interested in this market appraisal and would like to find out the causes if there is a decline in the ratio.

Thus the ratio reflects the price currently being paid by the market for each rupee of currently reported earnings per share.

Formula:
Price Earnings Ratio = Market price per share / Earnings per share.

Table 3. Price Earning Ratio

<table>
<thead>
<tr>
<th>Year</th>
<th>Earnings per share (Rs.)</th>
<th>Market price (Rs)</th>
<th>Price Earning ratio (times)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-2004</td>
<td>4.27</td>
<td>288</td>
<td>67.48</td>
</tr>
<tr>
<td>2004-2005</td>
<td>4.91</td>
<td>392</td>
<td>79.84</td>
</tr>
<tr>
<td>2005-2006</td>
<td>11.78</td>
<td>265</td>
<td>22.50</td>
</tr>
<tr>
<td>2006-2007</td>
<td>29.18</td>
<td>361</td>
<td>12.37</td>
</tr>
<tr>
<td>2007-2008</td>
<td>42.87</td>
<td>284</td>
<td>6.62</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Dalmia Cement (Bharat) Limited.

The price earnings ratio has decreased from 67.48 in 2003-2004 to 6.62 in 2007-2008. This is a good news for the investors as it implies that they have made wise investments for in 2004-2005 the ratio was as high as 79.48, implying that the investors were paying more i.e., 79.48 for each rupee of earnings per share as compared to the year 2007-2008 when they paid 6.62 for each rupee of earnings.

MARKET VAULE TO BOOK VALUE RATIO

Market value to book value ratio is the ratio of the share price to the book value per share. This ratio helps in determining the net worth of the company as compared to the amount the shareholders have invested in the company. In other words it enables a comparison between the amount actually paid by the shareholders and worth of each share.

Formula:
Market value to book value ratio = Market value per share / Book value per share

Book value per share = Net worth / Number of shares
Net worth=Share capital+Reserves
Table 4. Market Value to Book Value Ratio

<table>
<thead>
<tr>
<th>Year</th>
<th>Market price (Rs)</th>
<th>Book Value (Rs)</th>
<th>Market value to book value ratio (times)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-2004</td>
<td>288</td>
<td>5.73</td>
<td>50.26</td>
</tr>
<tr>
<td>2004-2005</td>
<td>392</td>
<td>5.79</td>
<td>67.70</td>
</tr>
<tr>
<td>2005-2006</td>
<td>265</td>
<td>5.95</td>
<td>44.53</td>
</tr>
<tr>
<td>2007-2008</td>
<td>284</td>
<td>7.03</td>
<td>40.40</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Dalmia Cement (Bharat) Limited.

The ratio has been fluctuating over the years from 50.26 in 2003-2004; it increased to 67.70 in 2004-2005. This is due to the fact that while the book value increased due to the increase in reserves the market price had not significantly increased. Thus while book value has increased over the years the market price has own wide variations and so the ratio has been on an increased implying that the shareholders are paying higher over the years for the shares of the company whose net worth is increasing.

RETURN ON EQUITY

The equity shareholders are the real owners who bear all the risk, participate in management and who are entitled to all the profits remaining after all outside claims including preference dividends are met in full. The return on equity is the single most important ratio to judge whether the firm has earned a satisfactory return for its equity shareholders or not. Its adequacy can be judged by comparing it with past records or by comparing it with overall industry average.

Formula: Return on Equity=Net profit after tax/Net worth.
Net worth=Share capital+Reserves.

Table 5. Return on Equity

<table>
<thead>
<tr>
<th>Year</th>
<th>Profit after tax</th>
<th>Net Worth</th>
<th>Return on Equity(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-2004</td>
<td>254.00</td>
<td>4017.00</td>
<td>6.32</td>
</tr>
<tr>
<td>2004-2005</td>
<td>309.00</td>
<td>4743.00</td>
<td>6.51</td>
</tr>
<tr>
<td>2005-2006</td>
<td>848.00</td>
<td>6506.00</td>
<td>13.03</td>
</tr>
<tr>
<td>2006-2007</td>
<td>2289.00</td>
<td>11426.00</td>
<td>20.03</td>
</tr>
<tr>
<td>2007-2008</td>
<td>3472.00</td>
<td>16452.00</td>
<td>21.10</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Dalmia Cement (Bharat) Limited.

The return on equity was the highest in 2003-2004, because the profits in 2003-2004 increased to 254 as income from sale of cement in market rapidly increased in 2003-2004. The return on equity was the lowest in 2005-2006 for there was no major increase in profits while the reserves continued to increase due to higher retentions.

GROWTH IN EQUITY

Generally the shareholders are more interested in the dividend per share than in the earnings per share. For dividend is the income that they actually receive. The earnings, which are not distributed to the shareholders, are retained in the business. This retention ratio along with the return on equity helps in determining the growth in equity.
**Formula:**
Growth in Equity = 
Retention Ratio $\times$ Return on Equity.
Retention Ratio = 1 - Payout Ratio
Return on equity = Net profit after tax/Net worth

### Table 6. Growth In Equity

<table>
<thead>
<tr>
<th>Year</th>
<th>Return on Equity (%)</th>
<th>Retention Ratio (%)</th>
<th>Return on Equity (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-2004</td>
<td>6.32</td>
<td>-17.10</td>
<td>-1.08</td>
</tr>
<tr>
<td>2004-2005</td>
<td>6.51</td>
<td>-1.83</td>
<td>-0.12</td>
</tr>
<tr>
<td>2005-2006</td>
<td>13.03</td>
<td>83.02</td>
<td>10.81</td>
</tr>
<tr>
<td>2006-2007</td>
<td>20.03</td>
<td>89.72</td>
<td>17.97</td>
</tr>
<tr>
<td>2007-2008</td>
<td>21.10</td>
<td>90.67</td>
<td>19.13</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Dalmia Cement (Bharat) Limited.

The retention ratio has been high from 2005-2006. The growth in equity in respect of other years has been declining owing to the decrease in retention ratio. The growth peaked in 2007-2008 when there was a rapid increase in profits while the retention was also high.

**FINDINGS:**

1) Dividends declared by a firm satisfy the shareholders need for current income and such dividend income will not be taxed in the hands of the shareholders.
2) The company has followed a stable dividend policy over the years. The company has paid regular dividends.
3) Regular payment of dividends sends out positive signals to the shareholders as it implies that the management foresees an increase in the future earnings of the company.
4) The average payout over the past 5 years has been 10.674%.
5) The payout of 10.674% is low but generally high growth companies tend to make low payments due to the various investment opportunities available.
6) The dividend yield and earnings yield have been on the increase implying that the returns of the shareholders in relation to the market price is on the increase.

**SUGGESTIONS**

1) Analysis believe that if the return on equity is more than 15% then the investors would prefer retained earnings and reinvestment for such earnings.
2) In case of growth companies like Dalmia it is believed that investors would prefer stock dividends and stock splits but the importance of cash dividends as a regular source of income and the added tax benefit cannot be ignored.
3) It is essential for the company to continue with its current dividend policy of regular dividends and to go in for additional payments on special occasions to retain the confidence of the investors.
4) The company should gradually increase its payout for if it is unable to meet investor expectations in the future and there is reduction in the dividend declared it would adversely affect the reputation of the company.
CONCLUSION

The dividends declared by a company are a source of current income to the shareholders and especially benefit those shareholders who do not wish to dip into their capital and who would like to hold on their investments. Apart from this the tax benefit on dividend income cannot be ignored.

The general argument is that dividends declared by the company are only nominal and that the shareholder would be better off if the company retained it for further investments.

Dalmia Cement (Bharat) Limited has followed a regular dividend policy. The average payout of the company for the past 5 years is 10.674% while this payment is considerable low it is not unusual or a growth company to follow this policy as it has greater investment opportunity but the bonus on the company to ensure a gradual increase in the dividend declared as it implies that the management foresees a bright future for the company.

REFERENCES


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2) www.economictimes.com
3) www.nifty.com

Reports