Dividend Policy

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1. Introduction

1.1 Preface

Dividend payout policy is one of the most important topics in the corporate finance. The profits generated by any organization are distributed for investment and consumption purposes in accordance with the dividend policy. The term "dividend policy" is associated with the distribution of profits of public limited companies. In a broader sense, the term "dividend policy" can be understood as a mechanism for the formation of the share of profits paid to the shareholders, in accordance with the share of his contribution to the total amount of the company's share capital.

1.2 Objectives

The primary objective of the management is to ensuring the maximization of wealth of the shareholders. Payment of dividend leads to increase in the price of shares on the one hand but leads to a crunch in liquid resources for financing of prospective projects. There is an inverse relationship between dividend payment and retained earnings. The major objectives of dividend policy are to:

- Ensure maximization of wealth
- Maintain future prospect
- Maintain stable rate of dividend
- Ensure degree of control over payout ratio

1.3 Scope of the manual

Dividend policy refers to the decision of the board regarding distribution of residual earnings to its shareholders. The broad scopes of the policy are as follows.

- Factors affecting dividend policy
- Mode of dividend
- Determinants of dividend policy
- Types of dividend policy
- Impact of key financials
- Process of Dividend declaration
- Role of the Board
- Role of the shareholders
- Accounting treatment regarding dividend
- Dividend distribution policy

2. Factors affecting dividend policy

When deciding on the dividends to pay out to shareholders, one of the main considerations of the Board of Directors will be the amount of earnings they wish to retain to meet financing needs. As well as future financing requirements, the decision on how much of a company's profits should be retained, and how much paid out to shareholders, will be influenced by:

a) Liquidity
b) Investment opportunities
c) Investor's preference
d) Target capital structure
e) Availability of external capital:
    i. Borrowing capacity
    ii. Access to capital market
    iii. Restriction in loan agreements/bond indenture
    iv. Legal restriction
f) Control
g) Inflation

3. Mode of dividend

There are various forms of dividends that are paid out to the shareholders:

3.1 Cash Dividend

A Cash dividend is the most common form of the dividend. A cash dividend is the distribution of funds or money paid to stockholders generally as part of the corporation's current earnings or accumulated profits. A company's Board of Directors announces a cash dividend on a declaration date, which entails paying a certain amount of money per common share. After that notification, the record date is established, which is the date on which a company determines its shareholders on record who are eligible to receive the payment. The dividends are allotted to the shareholders after the dividend is approved in Annual General Meeting (AGM).

3.2 Stock Dividend

Stock dividend also known as scrip dividend or bonus shares is a distribution of shares to existing shareholders in lieu of a cash dividend. This type of dividend may be made when a company wants to reward its investors but doesn't have the spare cash or wants to preserve its cash for other investments. Bonus shares are issued by the company when they have low operating cash, but still want to keep the investors happy. Each equity shareholder receives a certain number of additional shares depending on the number of shares originally owned by the shareholder. The market price, EPS, DPS etc. will be adjusted due to diluted effect.

3.3 Other modes of dividend

There are other forms of dividend also subject to the regulatory approval and within legal framework.

4. Determinants of dividend policy

Some determinants of dividend policy are discussed below:

4.1 Dividend pay-out ratio:

Dividend pay-out ratio is calculated by dividing the dividend per share by earnings per share. It indicates the proportion of earnings distributed as dividend. Lower dividend pay-out ratio indicates conservative dividend policy. However, high dividend pay-out ratio shows liberal dividend policy which may put a question mark over financing of future projects.

4.2 Stability of Dividend:

Shareholders prefer a stable dividend policy which means they require a certain minimum percentage of dividends to be paid regularly to them. Therefore, dividend policy should be devised taking into account this aspiration of the shareholders.

4.3 Liquidity:

The liquidity position of a company affects the dividend policy. Payment of dividend requires availability of cash resources. Future investment opportunities should also be taken into consideration.

4.4 Divisible Profit:

Dividends can be declared out of revenue profits but not out of capital profit. This means dividend can be declared out of divisible profit, i.e. the profit which is legally available for distribution as dividend to the shareholders. In certain cases, capital profit may be distributed as dividend if it is realized in cash and it is permitted by the articles of association.

4.5 Capital Market Conditions and Inflation:

Capital market conditions and inflation play a domi-nant role in developing the dividend policy. A company having an easy access to the capital market will follow a liberal dividend policy in comparison to others. During times of inflation a good com-pany tries to satisfy its shareholders by paying higher dividends.

4.6 Shareholder’s Consideration:

Tax statuses of shareholders, availability of investment opportunities, ownership dilutions, etc., are the different factors that affect shareholders. These factors should be taken into consideration while devising a dividend policy.

5. Types of dividend policy
There are different types of policies related to the dividend which the company can follow. Four most prevalent types of dividend policy are –

5.1 Regular Dividend Policy:
Under this type of dividend policy, the company follows the procedure to pay out a dividend to its shareholders every year. If the company earns abnormal profits, then it retains the extra profit. Whereas, if it remains in loss any year, then also it pays a dividend to its shareholders. This type of policy is adopted by the company who are having stable earnings and steady cash flow. In the eyes of investors, a company paying regular dividends are low risk despite the fact the quantum of regular dividend might be small.

5.2 Stable Dividend Policy:
Under this type of dividend policy, the company follows the procedure to pay out a defined fixed percentage of profits as dividends every year. For example, suppose a company sets the payout rate at 10%. Then this percentage of profit will be paid out as dividends every year regardless of the quantum of profit.

5.3 Irregular Dividend Policy:
Under this type of dividend policy company states that it has no obligation in respect of paying a dividend to the shareholders. The board of directors will decide the quantum and rate of dividend. They will decide in respect of action, taken with the earned profit. Their action in respect to paying a dividend has nothing to do with the company's scenario of earning a profit or coming into the loss. It depends on the decision of the board of directors.

5.4 Zero Dividend Policy:
Under this type of dividend policy, the company follows the procedure of paying no dividend to the shareholders irrespective of its profit or loss scenario. The payout ratio will be 0%. The total earning will be retained by the company. It will reinvest into the company model of business to expand it further with an increased rate and without hurdling into issues like liquidity.

6. Impact of key financials
Financial ratios have a significant impact on dividend declaration. Management analyzes the key financials and based on that; dividend payout ratio is determined. Some common financials are responsible for dividend pay-out:

- Net profit
- Earnings per Shares (EPS)
- Capital Adequacy
- Maintenance of sufficient provision against classified loans and advances
- Return on Equity
- Retained Earnings
- Paid up capital
- Shareholder's Equity
- Others

7. Process of Dividend Declaration
The management will determine the financial ability that defines how much dividend Bangladesh Finance should distribute to its shareholders, what the impact will be on share prices of the company and what will happen if the amount of dividend changes from year to year. Based on the financial analysis, the mode of dividend is determined whether it will be cash or stock. Capital adequacy is another key factor for determining the dividend mode. The dividend is proposed hereby by the Board of directors meeting and subsequently declared at Annual General Meeting (AGM).

8. Role of the Board
The Board of directors plays an integral role regarding dividend proposition. The recommendations made by the Board should be aligned with the greater interest of ordinary shareholders and the company. The Board proposes cash or stock form of dividend subject to approval in Annual General Meeting (AGM).

9. Role of the Shareholders

Ordinary Shareholders are the ultimate beneficiary of dividend. In line with the Board proposition, shareholders are responsible to give their prudential recommendation of dividend in Annual General Meeting (AGM). Once the shareholders approve the proposed dividend in AGM, the dividend becomes declared dividend.

10. Accounting treatment regarding dividend

Dividends are taxable income for shareholders. Depending on the entity, tax is deducted from the final dividend payment. Relevant accounting entries are made in accounting book and financial statements as per IAS and IFRS.

11. Dividend Distribution Policy

Bangladesh Finance shall follow the rules and guidelines regarding distribution of dividend as prescribed by the regulatory authorities. Cash dividend shall be paid directly to the entitled shareholders' bank accounts as available in the BO accounts maintained with the depository participant (DP), or the bank accounts as provided by the shareholders or unit holders in paper form, through BEFTN with 30 days of final approval by the shareholders in the AGM.

Upon receiving the detail information and claim on cash dividend from a stock broker or a merchant banker or a portfolio manager for the margin client or customer who has debit balance or margin loan, the cash dividend shall be paid to the Consolidated Customers' Bank Account (CCBA) of the stock broker or to the separate bank account of the merchant banker or portfolio manager.

Cash dividend shall be paid off to the non-resident sponsor, director, shareholder, unit holder or foreign portfolio investor (FPI) through the security custodian in compliance with the rules or regulations in this regard.

In case of non-availability of a valid bank account or not possible to distribute cash dividend through BEFTN or any electronic payment system, cash dividend warrants shall be issued and sent by post to the respective shareholders' addresses.

For the purpose of paying dividend, a separate bank account shall be maintained from which all the dividend payments are being made. Again, any unpaid or unclaimed cash dividend including accrued interest (after adjustment of bank charge, if any) thereon, if remains, shall be transferred to a separate bank account of the issuer as maintained for this purpose, within 01 (one) year from the date of declaration or approval or record date, as the case may be.

Stock dividend shall be directly credited to the BO accounts of respective shareholders within 30 days of AGM (final approval) or record date, as the case may be subject to clearance of the exchange(s) and Central Depository Bangladesh Limited (CDBL). The stock dividend shall be allotted within 60 days of AGM.
The company shall inform its shareholders through publication in the newspaper after the dividend is being disbursed or credited. Besides shareholders on record date shall be intimated through short message service (SMS) to the mobile numbers or email addresses as provided in the BO account.

12. Conclusion

This policy described here is solely created as internal dividend policy of Bangladesh Finance Limited. Authority has the right to change any clause of the policy if required.