

The Dividend Politics of Romanian Enterprises

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Abstract

The dividend politics – a managerial option of any entity between partial re-investment and total re-investment of the net profit and/or total or partial distribution of this one in the form of dividends. For a good management we have the problem to choose between the dividend and the auto-financing. The allocation of a big amount of the net profit as dividend limits the possibilities of auto-financing of the society and manages to the rise of the degree of obligation. On the other hand, a society which practices a politics of dividend characterized by a high rate of dividend enjoys of the appreciation of his actions on the market, and this fact has as consequence the rise of the possibilities of financing through new emissions of actions. The choice of one of these alternatives or the possibility of the effectuation of combinations between them is governed by the major demand of the finances – the maximization of the value of the entity.

Keywords: dividend, residual dividends, extra-dividend, rate of dividend, investing behavior

1. Introduction

Two big theorists of the finances, Merton Miller and Franco Modigliani elaborated, at the beginning of the '60, the theory of the insignificance of the dividend, which affirms that the dividend politics has no effect neither on the market price of the actions, nor on the cost of the capital. The two theorists explained that the value of an enterprise depends only on the income generated by her actives, and not on the manner of repartition of this income between dividends and the proper founds of financing. The conclusion of these two was that as a result of granting the dividends, the society must advance supplementary social capital in order to finance the activity in accordance with the previously established budget. This way, the rise of the dividend for an action is neutralized by the rise of the number of actions possessed by the owners, the price at the market changes not.

The two theorists based their arguments on a lot of "caeteris paribus" conditions, as if the inexistence of the emission or of the transaction costs, the null value of the income tax, the total transparence of the information concerning the perspectives of the enterprise, the distribution of the incomes with no effect on the costs of the own capital of the enterprise, etc.

The theory of Miller and Modigliani received an opposition from other two financing theorists, Myron Gordon and John Lintner, who appreciated that the investors are more attracted by the payment of dividends as by the eventually gains of the enterprise following the reinvestment of

the obtained profit. According to this two, the investors give a bigger value to a dollar from dividends as to a dollar from estimated capital gains.

The argument of Gordon-Lintner was called by Miller and Modigliani the mistake of "the sparrow in the hand" because the majority of the investors plan anyway the reinvestment of the amounts received as dividends in actions in the same enterprise or in similar enterprises. According to these two, the degree of rescues of the hard cash depends only on the activity of the enterprise, on the operational tides and not on the politics of the dividend.

These two theories offer contradictory advices to the managers of companies. That empiric testing has not given any clear conclusion because of the fact that the hypotheses on which are based exists not in the practice. In Romania, the instability of the national currency and the low degree of maturity of the capital market, as well as the predisposition of the investors to receive fast gains are turning the dividend into an attractive object, which leads to the appreciation in the market of the actions emitted by the societies offering the dividends.

2. The dividend politics

The dividend represents the part of the profit of a joint-stock company, which amounts to any stockholder in relation with the actions he possesses. For the investors on the stock exchange market, the politics of dividend practiced by the societies became an important standard for the adoption of the investment strategy. This obtains a more and more bigger importance for the persons who don't like the rescue, who save the available money through the capital market as an alternative for the banking system. At the same time, the entities according the dividends are interesting as well for the other investors with a bigger inclination to the rescue, with a bigger supplementary amount as the gains of the differences of the rate.

But the politics of dividend is the one which determinates the distribution of the profits obtained in payments to the shareholders and restrained funds in order to reinvest them in the business, therefore the one which establishes the rate of the dividend, a rate to be calculated through the report in percents between the sum of the net profit distributed to the shareholders in the form of the dividends and the value of the net profit.

For the management of any entity we confront with the problem of choosing between the dividend and the auto-financing. The attribution of a big rate from the net profit as dividend restrains the possibilities of auto-financing of the society and manages to the rise of the degree of obligation. On the other hand, a society which practices a politics of dividend characterized by a high rate of dividend enjoys of the appreciation of his actions on the market, and this fact has as consequence the rise of the possibilities of financing through new emissions of actions.

According to the legal stipulations, the dividends are given only one time for a financial year, and this fact after the end of the financial year, which, in our country is the same as the calendar year, so that the dividend of the profit obtained by the enterprise for that year is given the next year. At the same time with the General Assembly of the Shareholders (which usually take place before April including), where are analyzed the financial results of the society for the past year, it is also established the manner of conceding the dividends. In practice for the unfolding of the General Assembly of the Shareholders it is published a summons to fix, at the proposal of the Administration Council a reference date, a date which must be after the publication of the summons and which serves to identify those shareholders who can decide in the General Assembly of Shareholders concerning the dividend politics of the society.

These are the ones who can receive the dividends in the case they are voting the grant of dividends. Between the date of publishing of the summons and the date of the unfolding of the General Assembly of Shareholders must elapse 15 days.

Also in the General Assembly of the Shareholders where they are voting the grant of the dividend must be established the date to make the payments, but also the manner to pay the dividends.

In the practice, in establishing the politics of the dividend, the managers of a society must take care of the fact that the announcement of one dividend estimated for the future represents an engine of rise of the prices of the actions on the market. The appreciation of these actions on the market is motivated, except the dividend estimated to be given, also by the fact that the estimations on the dividend represent a signal of future profits, of tides of cash with positive clearance sale. On the other hand, the management can't ignore the preferences of more important shareholders. This way, a shareholder found of investment can choose a bigger rate of the dividend, to the detriment of the amount of profits given as a source of investments or financing of the activity of the society. Another shareholder can not pay so much attention to an immediate gain from dividends, but sustain fervently the reinvestment of a bigger part of the net profit.

In the states with developed capital market there are practiced more politics of dividend, so that the managers can choose alternative variants of distribution of the net profit obtained by the society, satisfying one category or another of shareholders. In the practice, the entities can use, in function of the economic context or of their business opportunities alternatively any politics of dividend.

The politics of the residual dividends – according to which an entity, in order to decide the proportion of profits distributed in the form of dividends must follow the four steps: the determination of the optimal investment budget, the determination of the necessary capital for the financing of this budget; the utilization of the profits accumulated in the own capital, as much as possible and the payment of dividends only if the obtained profits are bigger than the necessary ones in order to realize the planed investments.

This method comes from the premise that the investors prefer that the enterprise retain and reinvest the profits, if the rate of profit obtained after this reinvestment is bigger than the rate of profit which the investors can obtain for another investments with a comparable degree of rescue. This politics of dividend will disappoint the people who prefer to receive one part of the net profit in the form of dividends. Shortly, this theory which affirms today the managers, considers that the politics of dividend is not a very important financial decision. The central idea of this theory is to use, with priority, the profit retained for the auto-financing of the investment projects, as many times as the counted profit of these ones is bigger than the costs of the capitals of the entities, obtaining this way a maximization of the value of these. We can say this way that the optimal politics of dividend is the one of the reinvestment of the total profit.

Constant or progressive rising dividends – means the grant of dividends in constant amount or with a constant rate of rising, which usually adjust with the rate of the inflation. Through the manner of function, the grant of the dividends supposes generally speaking economic and currency stability. For this reason it is practiced more in the developed countries.

The reasons at the base of that politics are in nature to attract the investors, counting on their preference for the stability. This way the investors accord a bigger value to the dividends, which they are sure they will receive. The fluctuant dividends have a raised degree of rescue and this fact determine a lower appreciation on the market of these actions. On the other hand, a lot of shareholders utilize the amounts they receive as dividend for current expenses and they

prefer to plan their expenses in function of stable amounts. They can be in unpleasant situations if they are forced to liquidate a part of what they detain in order to have cash money.

The constant rate of the dividends – a politics of dividends is characterized by the distribution in form of the dividends in a constant proportion of profits. The politics of distribution through a constant rate of the dividends is a disadvantage of the investors when the profits are low. In the same time it has not a big degree of predictability as the politics of the progressive raising dividends, but it realizes a compromise between the interests of the entity and those of the shareholders. On the one hand, the society can better administrate the profits it obtains and not support the burden of a dividend fixed on the periods with a lower profit (it can better plan the future investments and the engagements with the purveyors). On the other hand, the investors, even if they are not expected at a constant amount given as divided, they can estimate the dimensions of this one in function of the quarterly profits registered by the entity, corroborated with the budget of amounts and expenses. For example, if the stipulations of the budget of amounts and expenses regarding the net profit are surpassed at the end of the third quarter, the chances that the whole profit estimated to be realized are raised and, as consequence, the investors can estimate the value of the dividend which they follow to receive, being this way accomplished the demands of the entity regarding a good auto-financing, as well as the predisposition to stability of the investors.

The regular dividend with a low value and the surplus – such a politics of the dividend represents in fact a compromise between the payment of a stable dividend or a dividend with a stable rate of raise and a constant proportion of the profit distributed in form of the dividends. For the entity, the advantage is a bigger flexibility and for the investors the assurance to cash at least a little amount for the regular dividend, so that it could be paid even in the years with little profits and then supply this amount with an extra-dividend, in the years when excessive funds are available. This supplementary dividend means a real signal for the investors that the society obtains considerable profits. If the entity pays that supplementary dividend year after year, the payment becomes a habitude for the investors. Its elimination can have as effect the diminution of the price of the actions on the market, even if at the beginning it was seen as a surplus.

In function of the size of the dividend, the entities can be categorized in one of the three types of the dividend politics:

- ✚ *The politics of direct participation at the realization of the profit*, based on the assurance of a relatively constant rate of distribution of the dividends, where the size of the distributed dividend is variable in function of the size of the obtained profit and the shareholders have a direct amount of participation at the profit.
- ✚ *The politics of stability or prudence*, where the entity has as proposal to assure a constant dividend or a constant rate of yearly raise of the dividend, doesn't matter the variations of the size of the profit.
- ✚ *The opportunist politics*, where the size of the dividend is in function of the decision of investment and of the decision of financing.

In our country, the clear definition of a dividend politics is hard to realize, as far as concerns the particularities of the Romanian industry. A lot of entities with productive activity are confronted with fixed actives, used physically and morally and with the supra-dimension of the work. All this facts need restructure, which make difficult to establish a plan on long term regarding the dividends. Otherwise some of these entities with a big size have earned significant debts to the state budget or to the budget of the social assurances. Until now, the financial societies (S.I.F., banks) or the assurance societies realized the establishing of some practices regarding the dividend, which are very near to a politics of the dividend relatively coherent.

In the application of one of the possible forms of politics of dividend that we announced, we must take care of the factors of influence on these ones:

- + *the juridical settlements in a continual modification;*
- + *the availability of the hard cash* – a crisis of liquidities can cause difficulties to grant that ones, sometimes the entity can be forced to contract banking loans.
- + *the debts of the entity* – in the case of some historical bigger debts, the entity has the normal tendency to retain a bigger amount of the profits obtained for the payment of these ones. This way the sum purposed as dividends will be lower or even null.
- + *the possibility of the acceleration or the adjournment of the projects of investment* – this fact will avoid to an entity to respect easier the politics of dividend established further.
- + *-the effects of the dividend politics on the costs of the capital* - the managers must take care while adopting a decision regarding the grant of dividends at the manner are appreciated at the market the actions of a society with a stable politics of dividend as well as at the manner to constitute this politics in a mechanism of signalization of the results of the society.
- + *the degree of concentration of the actions and the preferences of the shareholders* – the social capital of some societies is concentrated in the hand of one shareholder or a group of shareholders. Their preferences guide while adopting some practices regarding to grant the dividend. This way, if for example, the major shareholder is a society of financial investments, which at its turn prefer to pay the dividends to its shareholders, the entity will then adopt a stable practice of payment of the dividends. It is to be knew also the fact that the entities where the major shareholder is the Employers Association (the majority of those people bought actions with the payment in rates), gives usually dividends in a big proportion of the net profit.

In order to follow the dividend politics of an action society, to create the possibility to compare it with other similar entities or to take evidence of the performances of the different entities regarding the politics of dividend can be used different indicators that we can enumerate here:

- + the dividend on an action – it measures the absolute sum of the dividends distributed for an action detained;
- + the rate of distribution of the dividends – signalizes the rate of the distribution of the dividends;
- + the efficiency on one action – indicates a high economical expressivity, with a big interest for the shareholders and because signifies an authentically efficiency of the capital placed in actions;
- + the profit on one action – represents the practical enrichment of the shareholders in the course of one year because the profit will be distributed as dividends or it will be capitalized, representing also the property of the shareholders.

It has been presented some perspectives on which depends the politics of dividend of one entity, without having the pretention to cover all the factors of influence or to debate in a detailed way the mechanism of action on the decision of the management concerning the dividends.

3. Aspects of the politics of dividends in Romania

The practice of a dividend politics from the Romanian entities, after the European principle, is not entirely possible because of the instability of the currency, because of the law instability and of the degree of attrition of the fixed middles. If we follow therefore the evolutions of the last years, we can discover a similitude, from year to year, in establishing a rate of the dividend, of a rate of reference or of other aspects resembling to the politics of the dividend. More than that, at one analysis of the politics of the dividend in Romania we can constant that it is in course of development, but it is not on a high economic level as necessary. It doesn't matter the politics of dividend adopted by an entity in Romania, it is necessary to consider the rate of inflation extremely high of the last period. The payment through the dividends is only in

part satisfying, because the rhythm of the raise of these was low than the general indices of prices in Romania, so that the efficiency of the actions through the dividends can be negative, it not assure a valorization at a correspondent rate of the invested capitals, but can manage to a degradation of these ones in the time.

For the realization of a study of case I used some statistic facts and I selected a number of 20 entities classified in function of the stability of the rate of the dividend and of its size. I used the middle deviation, which can calculate the middle of the deviations from the arithmetic middle of these (a low deviation indicates a higher stability of the rate of the dividend. This deviation was divided to the arithmetic middle of the rates of the dividends in the last three years. So, here are explained the entities for which this report has the lower value and indicates a low deviation from a high arithmetic middle of the rates of the dividend (in order to keep the confidentiality of the dates I renamed the entities I have studied).

Entity / Company	Rate of the dividend			Arithmetic middle	Middle deviation
	2006	2007	2008		
Company Alfa	37,65	35,79	36,24	36,56	0,73
Company Omega	41,72	38,66	41,42	40,6	1,29
Company Beta	66,99	60,35	67,38	64,9	3,04
Company Urania	33,45	39,39	38,59	37,14	2,46
Company Select	65,80	76,96	77,81	73,53	5,15
Company Elegant	37,03	44,76	43,86	41,88	3,24
Company Familia	94,2	75,27	89,77	86,41	7,43
Company Prietenii	59,31	76,63	70,52	68,82	6,34
Company Nepoții	33,4	40,29	45,09	39,59	4,13
Company Fii	23,49	29,99	31,18	28,22	3,16
Company Fiicele	29,33	35,31	25,68	30,1	3,47
Company Asiatica	42,51	48,59	33,9	41,67	5,18
Company Europeana	20,29	15,98	23,81	20,03	2,7
Company Mondiala	62,94	87,55	67,78	72,75	9,86
Company Afacere	46,83	32,75	36,55	38,71	5,41
Company Cultura	16,36	15,44	21,72	17,84	2,59
Company Educație	32,48	31,15	43,94	35,86	5,39
Company Invățământ	27,95	48,8	36,33	37,69	7,4
Company Agricultură	31,24	23,78	43,66	32,89	7,18
Company Sport	11,22	7,24	6,89	8,45	1,85

It results that the society with the most stable politics of dividend is the Alfa Company, where really the rate of the dividends oscillated just a little around a value of 37%. The case of the Alfa Company must be analyzed while taking care of the fact that the major shareholder possesses 95% of the actions. This is interested to impose a politics of dividend stable to the societies which it controls, as a consequence of the fact that it must also pay its dividends.

The major shareholder of the Alfa Company possesses also 49,99% of the social capital of the Omega Company, which can explain its politics of dividend. Except the Omega Company, which has a destroyed structure of actions, the most part of the companies have a major shareholder who prefer, as we can see the security to receive a relative stable percent of the net profit as a dividend. So 7 of them have as major shareholder the Employed Association (Sport Company, Cultura Company, Mondiala Company, Invatamant Company, where there are two associations of the employers, which possess together more than 50% of the social capital – Select Company, Familia Company and Europeana Company).

Four companies have as major shareholder another company which possess the most part of the social capital, at the same time, for the two other societies the major shareholder is the state, through two of its ministries, with more than 66% of the social capital. For other two societies the significant shareholders are two persons who possess together more than 44% of the social capital, the dividend representing an important source of amounts.

Remarkable is the fact that some societies are keeping relatively stable the period of fixing the date of reference for the grant of the dividend. These are empiric observations and they are not imposing the security of the stability of the future reference dates. The Financial Investment Societies are received as the societies which practice the most stable politics of dividend. The grant of those in important proportions of the net profit and in rates relatively stables became already an habitude. But not all the societies give dividends in cash money.

For example, from 2003 to 2008, the Bank "Certitudine" preferred the grant of free actions as a consequence of the raise of the social capital from the reserves constituted from the net profit.

Period	2003	2004	2005	2006	2007	2008
Free actions at 100 detained*	49	63	45	68	80	36
Price of valorization** (lei/acțiune)	2750	1410	1620	1630	2650	3150
Net profit	6 530	12 782	26 317	36 465	44 272	-
Number of actions	5 000	10 000	17 370	39 616	71 309	97 086
Net profit per action (lei)	1,306	1,278	1,515	0,920	0,621	-

* the raise of the social capital of every year was realized through the incorporation of the reserves constituted from the net result of the last year

** the course of the market at 30 days after the date of the General Shareholders Assembly.

It is difficult and at the same time hazardous to make foreseeing, in the case of these societies, on the future level of the rate of the dividend (and, taking care of the evolution of the net result and of the stipulations of the budget of amounts and expenses, foreseeing on the level of the value of the dividend pro action). For all that, a player on the stock exchange cannot ignore the previous evolution of the practice of an entity regarding the grant of dividends and adjust the investment behavior calculating also this evolution.

4. Conclusion

At the level of any entity can be identified three financial politics, considerate at the beginning independent: the politics of investments, the politics of financing and the politics of the dividends. The alternatives of the decisions of the politics of investment are the specialization and the diversity of the activities while the alternatives of decision of the politics of financing are the internal and the external sources. The distribution of the dividends completes the image of a profitable entity, which can give money back from its own capitals. The constant distribution of the dividends manages to the raise of the investor's confidence in the entity, at the raise of the value of the entity on the market. The reinvestment from the raw profit manages to the raise of the financial autonomy, to the raise of the capacity of auto-financing, to the amelioration of the financial structure of the society's capitals. This way, the entity will have a superior financial potential of sustaining the own development, not only through auto-financing, but also the capacity to receive new credits. All this represent in fact factors of development and maximization of the value or the entity.

Because the alternative of the partial or entire reinvestment of the net profit in the financing of the projects of investment is a part of the politics of financing, we can say that the dividend politics is a part of the politics of financing. For a good management we have the problem to choose between the dividend and the auto-financing. The allocation of a big amount of the net

profit as dividend limits the possibilities of auto-financing of the society and manages to the rise of the degree of obligation. On the other hand, a society which practices a politics of dividend characterized by a high rate of dividend enjoys of the appreciation of his actions on the market, and this fact has as consequence the rise of the possibilities of financing through new emissions of actions. The choice of one of these two alternatives or the possibility to effectuate combinations between them is governed by the major demand of the finances – the maximization of the value of the entities. The principal objective of the financial management of an enterprise is the maximization of the value of the enterprise and can be realized:

- ✚ Through the maximization of the outputs of the enterprise;
- ✚ Through the minimization of the inputs of the enterprise.

The two ways of maximization of the value of the enterprise should not be regarded separately, but considerate permanently only together. From the financial perspective, the inputs become real in the components of the capital of the enterprise, its minimization consisting in the minimization of the costs of the different elements of the capital of the enterprise.

We will be able to see from this moment on that the first difficulties appear in the determination of the first costs for each of the specific components of the capital, and then, as a response at the managerial demands, at the level of the capital structure – in the form of the middle cost of the capital.

Otherwise, the decisions of financing are regarding three principal types of decisions:

- ✚ The choice of the structure of financing, which means the repartition between the capitals of the shareholders and those who come from the financial creditors. These decisions have a determinate influence on the size of the rescue supported by the shareholders. A raise of the obligation make grow the rescue for the shareholders.
- ✚ The politics of the dividends, that means the choice between the reinvestment of the profit and its distribution in the form of the dividends;
- ✚ The choice between the internal financing (auto-financing) and the external financing (the founs brought by the shareholders and the contracting of new financial debts).

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