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Dividends by diktat

Forced dividends and stock buybacks can't help in improving market perception of listed PSUs

To lend the economy a helping hand, should Central Public Sector Undertakings (PSUs) double down on capital expansion, step up dividend distribution rates or return capital through stock buybacks? Their promoter — the Government of India — appears to be quite confused in pressuring them to consider all three conflicting courses of action. In October, after conducting half-yearly performance reviews, the Centre ticked off energy PSUs for achieving less than a third of their capital expenditure targets for FY21 and urged them to exceed them by end of the year. Later in the same month, it was requesting eight PSUs to consider share buybacks to reward shareholders. Three PSUs have since announced buybacks totalling to over ₹4,200 crore. In November, it reminded PSUs of their obligation laid out in 2016, to pay out a minimum 30 per cent of their profit after taxes or 5 per cent of net worth as dividend and urged them to step up their distribution rates, even if it meant dipping into reserves. The above diktats appear to be aimed at improving abysmal market valuations of listed PSUs while helping their promoter bridge the fiscal gap but they may end up achieving neither objective.

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It is not without reason that listed PSUs trade at single-digit PEs and are seen as consistent wealth-destroyers amid the untrammelled bull run in Indian markets. Investors have taken an increasingly jaundiced view of the Centre applying one-size-fits-all criteria to periodically drain PSUs of their cash by way of dividends, buybacks and forced mergers. Today, PSUs such as Indian Oil Corporation and HPCL would be much better off conserving cash than paying out hefty dividends as they engineer a turnaround from the debilitating losses of the March quarter. NTPC and NMDC appear to be particularly poor candidates for stock buybacks. Both firms have been borrowing from the market — NTPC to bankroll its clean energy pivot and NMDC to fund its greenfield steel plant. NTPC and ONGC no longer boast debt-free balance sheets after forced stake acquisitions in disinvested PSUs. The Centre's missives to these PSUs is in direct contrast to RBI's recent directive to public sector banks to withhold dividend payouts this year to conserve capital; this appears a more prudent approach given the losses expected from Covid-related provisions later this year.

While there's nothing wrong in the Centre, as majority shareholder, asking PSUs to either put their cash to productive use or distribute it, the decision needs to be driven entirely by the commercial considerations of each enterprise, the state of the sector the firm operates in, its capex requirements and its ability to generate shareholder returns higher than capital costs. As a promoter looking to divest its stakes, the Centre has the most to lose if its cash demands impair the ability of sound PSUs to build capacities for the future and generate healthy shareholder returns, rendering them unappealing to investors.