25th September 2023

China's radical way of boosting dividend payouts

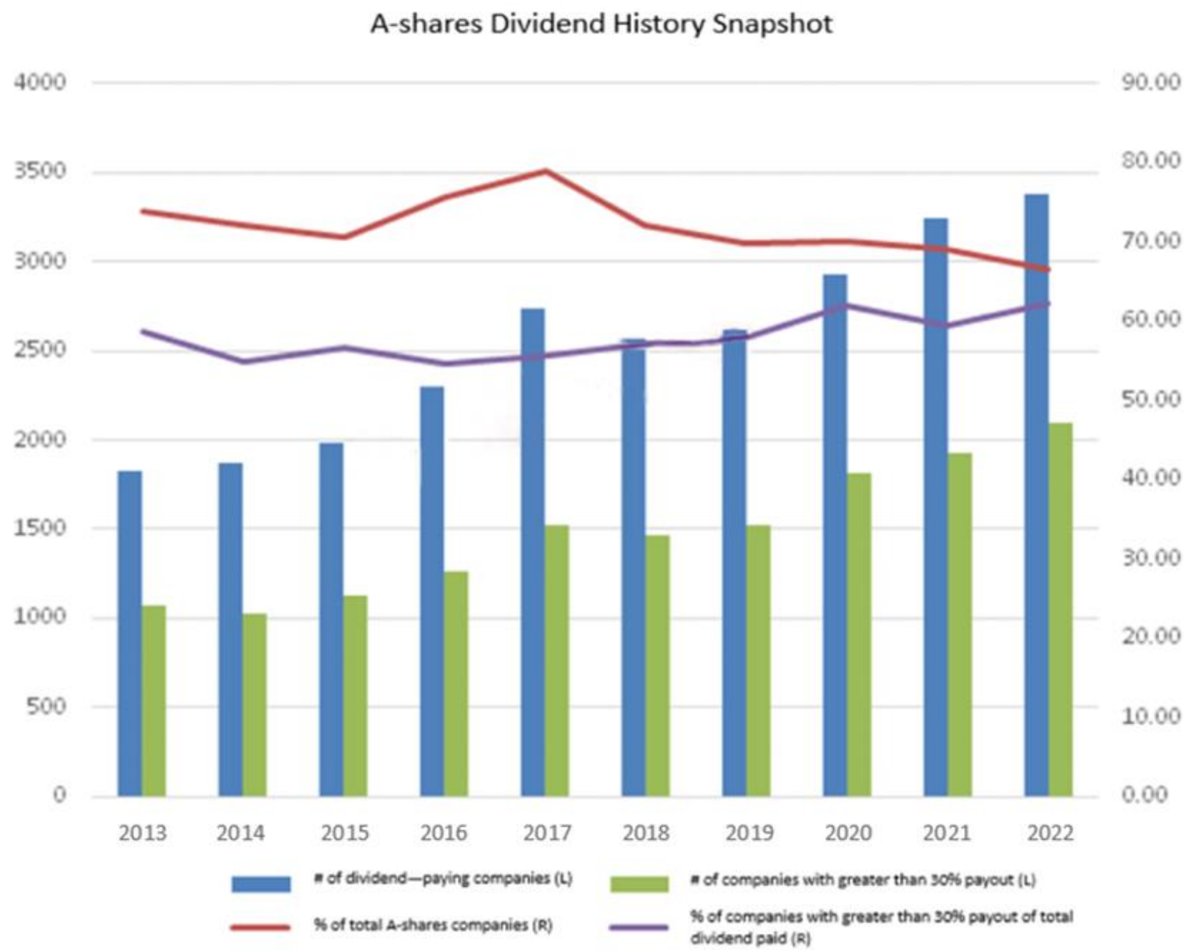
Facing a certain frustration expressed by retail investors against the poor performance of the Chinese A-share market, the market regulator China Securities Regulatory Commission (CSRC) has been actively rolling out a basket of measures to boost investor confidence during the second half of this year. Other than a widely reported 50% cut in stamp duty (from 0.1% to 0.05%), another critical measure was announced which raised quite a few eyebrows:

If a company's share price falls below its IPO price or below its book value, its controlling shareholder would be automatically prohibited from reducing his or her stake. Furthermore, the new regulation also prohibits controlling shareholders from selling their stocks if the company's average dividend payout ratio has been less than 30% over the past 3 years. This new regulation is not only expected to enhance the A-share market's overall investment return in the form of cash dividends, but it also aligns controlling shareholders' interests with those of minority investors.

We will dive into how A-share's dividend payouts have evolved over the past decade.

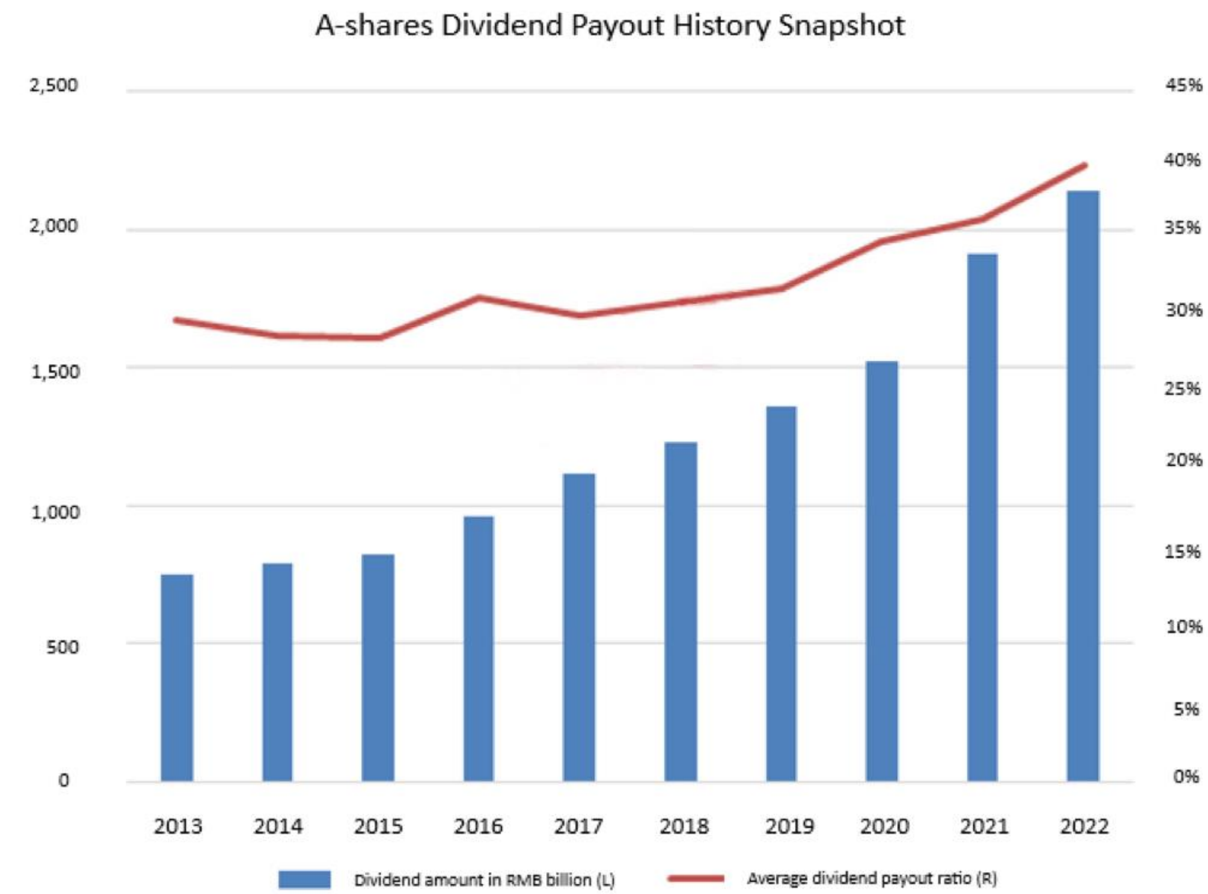
With the improvement of corporate governance practices and policy guidance issued over the past years by the market regulator, both the number of dividend-paying companies and the total amount of cash dividends paid have been on a steadily upward trend, although the percentage of mainland Chinese companies paying dividends came down a bit.

Back in 2013, 1,825 (74.0% of total) A-share companies were paying dividends. This number rose to 3,377 (66.7% of total) in 2022. Among the latter ones, those that had a dividend payout ratio higher than 30% reached 62.2% in 2022, the highest level in a decade. A simple back-of-the-envelope calculation would suggest that under the latest regulation described above, less than 40% of the A-share companies' controlling shareholders would be able to sell down their equity stakes as they wish. More than 60% of those controlling shareholders could not sell any share unless they alter their dividend policy.



Source: Securities Times

In terms of total amount of dividends paid, the A-share market had ten consecutive years of positive growth and reached the RMB 2 trillion mark in 2022, nearly three times as much as the total amount of dividends paid in 2013. In the meantime, the market's overall dividend payout ratio increased from 30.1% in 2013 to 40.3% in 2022. The fact that only less than 40% of the companies have a dividend payout ratio greater than 30% while the overall market's dividend payout ratio is above 40% suggests a very uneven dividend-paying pattern across different sectors in the A-share market.



Source: Securities Times

What are the high dividend-paying sectors?

According to statistics compiled by Securities Times, the banking sector has contributed the most amount of cash dividends, to the tune of over 4 trillion RMB in total over the past decade, with over 90% of the Chinese banks paying cash dividends on a regular basis. Other sectors such as non-bank financials, petrochemicals, food & beverage and coal mining are also ranked high on the list in terms of absolute payout amount.

In terms of payout ratio, companies in the food & beverage, communications, textile and apparel, coal mining, media, utilities, and home appliance industries had an average in excess of 50% in 2022.

It is also worth mentioning that in the A-shares market, state-owned enterprises (SOEs) have contributed the majority of cash dividends over the past decade, with a total amount close to RMB 9 trillion compared with a total RMB 2 trillion paid by the private sector. Although there are no statistically significant differences in payout ratios between SOEs and private sector companies, SOEs are likely to take the lead in further increasing payout ratios in the near future given CRSC's push of its rather esoteric "valuation system with Chinese characteristics" and its willingness to enhance shareholder returns.

On a company-specific basis, the big four Chinese banks (ICBC, Bank of Communications, Bank of China and Agricultural Bank of China) dominated the dividend-paying rank with a total payout of nearly RMB 3 trillion over the past decade, followed by the two petrochemical giants (Petrochina and Sinopec) and other state-owned banks. On the flip side, nearly 200 A-share companies never paid a single cash dividend over the last ten years, mostly due to poor profitability and high leverage ratio.

If this regulation that aims at normalizing dividend payouts is successfully implemented to align the interests of controlling shareholders with that of minority shareholders, we could expect to see noticeable improvements in both dividend returns and, more importantly, in investor confidence. It could ultimately attract more long-term investors to the market. Going forward, CSRC may consider rolling out more nuanced regulations in this area such as refining dividend mechanisms, implementing differentiated dividend policies for different sectors and optimizing dividend-related tax policies to further improve corporate governance practices and further boost investor confidence.