# Are Dividends Good or Bad?

*Perspectives: May 19th, 2025*

At face value, dividends are a simple concept, and they are always good, right?

Hold on. Not so fast.

At their best, dividends are wonderful. They are delivered directly into our pockets as a result of our participation in the economic profits produced by our companies. They can signal that a company is consistently producing free cash flows and that we are indeed part of a company. **But any good idea taken to an extreme can turn into a bad idea** .

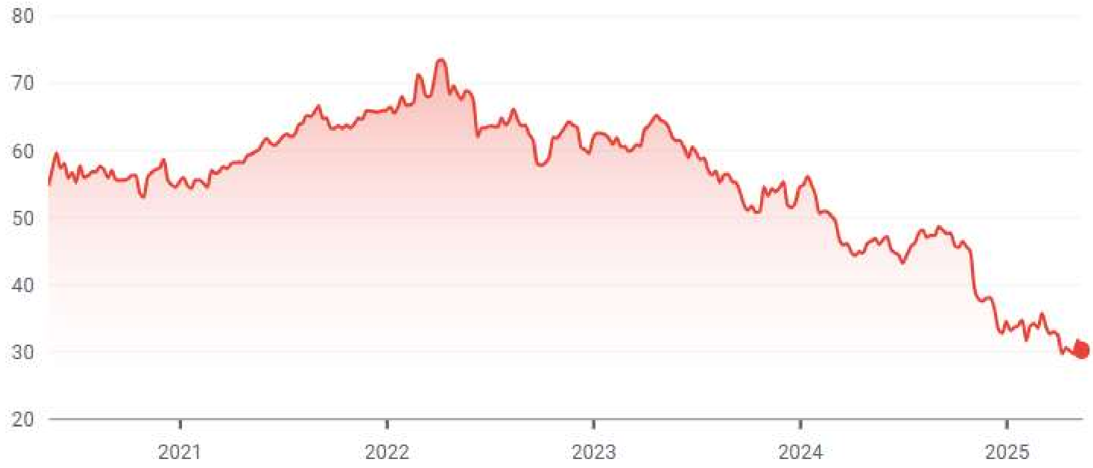
The Canadian listed telecommunications company **Bell Canada** is an informative case study. Income-oriented investors, typically pensioners, were attracted by its high trailing dividend yield. The problem they ignored were writ large on the wall – the company consistently paid out more in dividends than in earnings, combined with the balance sheet becoming increasingly leveraged while they also tried to acquire their way out of trouble. Unless the company had a hidden fairy godmother, this was unsustainable.

**Table: Bell Canada Earnings & Dividends Per Share** (*Source: Morningstar*)

| | EPS | DPS |
|---|---|---|
| FY2024 | 0,18 | 3,99 |
| FY2023 | 2,28 | 3,87 |
| FY2022 | 2,98 | 3,68 |
| FY2021 | 2,99 | 3,5 |
| FY2020 | 2,76 | 3,33 |

Predictably, it turned into a disaster. Despite management's persistent confidence expressed in the annual report as recently as March 2025, the dividend was eventually cut – significantly, but to no-one's surprise. The stock price had already more than halved since 2022 as income-oriented shareholders who had bought it purely for its high dividend yield became forced sellers.

Chart: Bell Canada Stock Price 2020-2025 *(Source: Google Finance)*




Perspective's long-term case study library contains a special folder for 'high dividend yield disasters'. A few more recent examples from around the world include 3M, City Lodge Hotels, and Pick 'n Pay. What these three have in common is a once genuinely great business becoming so infatuated with its hallowed status as a consistent dividend grower and payer that it ended up significantly harming the core business. Each one of them experienced tremendous hardship in acknowledging their reality and in overcoming their self-inflicted injuries, even needing capital injections by their shareholders and asset divestitures. In each case a strong new CEO had to clear the decks.

At their worst, paying excessive dividends can even turn into an existential risk. Our case studies clearly show how some companies slowly but surely put themselves under stress by steadily increasing their dividend payout ratio [*the percentage of profits being paid out as dividends*]. In some cases, such as Bell Canada, companies have in essence even resorted to borrowing money to pay dividends. That can easily be a fatal mistake.

Some listed companies and the media refer to dividends and share buybacks as being a 'reward' for shareholders. I understand why the phrase is being used, but this is a symptom of the agent-principal conflict, when so many listed companies are institutionally owned and professionally managed. Bell Canada's CEO earns C$13mn a year, while only owning C$4mn worth of the shares. Its largest shareholders, who own billions of dollars worth of it on behalf of their end clients, are large institutions with no board representation or management influence. Their collective army of governance analysts have made no difference whatsoever to management's poor decision making, the steady deterioration of the company, or the reality that the same management continued earning huge cash bonuses based on a scorecard.

True owner-oriented shareholders are not there to be 'rewarded' with a pat on the head. Owners are legally entitled to partake in the free cash flows of a company. Reducing it to essence, those free cash flows can only be directed to 5 things: Reinvesting in growth initiatives; Strengthening the balance sheet; Share buybacks; Dividends; and Shrinkage [*a term I am using to describe all forms of value leakage from shareholders to other parties*].

My point is that an overly simplistic focus on dividends and dividend yields can easily become costly investment mistakes.

Our work continues...

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