Share repurchase

Reasons for repurchases

• Information or Signaling Hypothesis
  ✓ No Profitable use for internally generated funds.
  ✓ Firm believe that stock is undervalued.
  ✓ Mixed results (positive or negative)

• Dividend or Personal Taxation Hypothesis
  ✓ In order to let the S/ Holders benefit from the preferential tax treatment of repurchases relative to dividend.
Residual Dividend Policy

Example
An analyst gathered the following information about a company’s investment plan:

- Capital Budget of Sh. 5 million
- Target capital structure is 70% debt and 30% equity
- Net income is Sh. 4 million

If the company follows a residual dividend policy, calculate the dividend payout ratio for this year?
Dividend Controversy

The Leftists

The leftist group believes that companies should avoid establishing a high payout ratio. They believe that such a high ratio is inconsistent with the policy of maximising the company's value as well as shareholders' wealth. Therefore, they believe that the company should adopt a low target payout policy in order to avoid affecting the company's value as well as the wealth of the shareholder in an adverse way.