Equity Research; Are 2020 dividends safe?

COLLINS SARRI STATHAM INVESTMENTS

Research Report

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Key Risks to Price Target

Not applicable

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Are 2020 Dividends safe? Not all of them

The pace of the Covid-19 2020 downturn has put company revenues, payroll, tax, debt servicing and fixed cost obligations under the spotlight.

The pressing issue is liquidity, how much cash does the company have access to? How much cash is needed to get over Covid-19?

Going into the Covid-19 problem, UK corporate cashflows were generally being optimized to maximise shareholder payments, make acquisitions, fund capital expenditure. But now companies must hunker down and delay capital decisions.

UK corporate cashflows are under severe pressure and facing an open-ended period that will see extra costs from business disruption, far lower revenues, declining profits and an intensifying competitive environment. Companies are likely to cut discretionary capital spending (including dividends) first, delay M&A plans and delay upfront corporate restructuring decisions.

Dividend payouts are an issue, but from a corporate viewpoint a relatively low priority one. Some stocks are indicating 'risky' 10%-17% dividend yields, when referenced to the old world of 2019. We expect 2020 will see significant payout changes / dividend deferrals/ scrip alternative offers as companies conserve cash.

Shareholders are not going to be pressing boardrooms in this strained environment, they have the same priorities, that the company gets through this tough, low revenue period with minimum debt accumulation and without too much permanent damage. No company wants pay shareholders out of scarce funds before having to draw on government financing shortly thereafter.

The sell-off has increased UK equity market 'yields', investors require higher yields and are placing a higher discount rate on payment expectations.

Company	FY19 Annual Dividend	DY (%) 20 March 2020	DY (%) 31 Dec 2019	Δ Change
Barclays	9p	10.0%	4.9%	5.2%
BATS	210.4p	8.1%	6.4%	1.7%
BHP Group	US$1.33	10.2%	6.3%	3.9%
BP	42 cents	13.6%	7.4%	6.2%
Carnival Corp	US$2.00	21.3%	4.7%	16.6%
Easyjet	43.9p	7.4%	3.1%	4.3%
Glencore	20 cents	14.0%	7.1%	6.9%
HSBC	51 cents	8.6%	7.2%	1.3%
IAG	60 cents	26.3%	8.2%	18.1%
Legal & General	16.21p	10.6%	5.2%	5.4%
Lloyds Banking	3.26p	10.5%	5.1%	5.4%
Royal Dutch Shell	US$1.88	15.1%	7.1%	8.0%
RBS	25p	22.0%	10.2%	11.8%
Vodafone	7.1p	6.0%	4.8%	1.2%

Source; CSS Investments Ltd

Dividend yields have surged during the sell off (from end 2019) – the selection of UK blue chips (above) have underperformed UK indices, which has moved from a 4.5% dividend yield to c. 7.25%.

Dividend growth over 2020 is a moot point at this stage. When viewed with the cash cost of dividends v free cash flow a clear picture emerges.

Company	Dividend Cost	Free Cash Flow	COMMENT/ VERDICT
Barclays	£1.55bn	Stable	CEO Jes Staley, subject of FCA probe promised 9p, hence high risk / CUT
BATS	£4.8bn	Stable	BATS wants to keep the payout despite structural problems / HOLD
BHP Group	US$2.8bn	Negative	BHP will post lower oil revenues but iron ore, copper is stable/ HOLD
BP	US$8.5bn	Negative	Cashflows under intense pressure, given Brent <$30/ bbl / CUT
Carnival Corp	US$1.39bn	Negative	Revenues under intense pressure over Q2, Q3 / CUT
Easyjet	£174m	Negative	Revenues under pressure, EZJ paid 2019 dividend, but in 2020? / CUT
Glencore	US$2.66bn	Negative	Expect GLEN to maintain dividend largely funded by debt/ HOLD
HSBC	US$10.36bn	Stable	Low US rates will hurt NIM, but payroll savings will fund payout/ HOLD
IAG	€1.29bn	Negative	Revenues under intense pressure, expect dividend cut/ CUT
Legal & General	£1.05bn	Negative	Business will be impacted by bulk annuity demand, but dividend HOLD
Lloyds Banking	£2.37bn	Negative	Board likely to hold dividend at current levels/ HOLD
Royal Dutch Shell	US$14.7bn	Negative	Cashflows under intense pressure, share scrip alternative is likely/ HOLD
RBS	£3.03bn	Negative	NIM under severe pressure/ CUT
Vodafone	£1.9bn	Stable	Board cut dividend prior to crisis hence expect dividend / HOLD

Source; CSS Investments Ltd

There is a "the more the merrier" aspect to this, so far Berkeley Group has cancelled its 400p special payout to conserve cash, Crest Nicholson cancelled its dividend the day it went XD (the first time I can recall this occurring). National Express said its dividend was under review ahead of ex dividend on 23rd April 2020.

Conclusion

Clearly the longer this environment persists, the higher the risk to payouts. Investors may be a bit in denial about the potential for dividend cuts over 2020. There is ample scope for surprises on dividends as cashflows are repositioned or as boards make decisions on drawing down government funding.

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BHP Group	**Relevant disclosures:** <2>
BP	**Relevant disclosures:** <2>
Berkeley Group	**Relevant disclosures:** <2>
Crest Nicholson	**Relevant disclosures:** <2>
Carnival Corp	**Relevant disclosures:** <2>
Easyjet	**Relevant disclosures:** <2>
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HSBC	**Relevant disclosures:** <1,2>
IAG Group	**Relevant disclosures:** <1,2>
Legal & General	**Relevant disclosures:** <2>
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