Dividend Investors: DH Corp. Slashes Dividend

Description

DH Corp. (TSX:DH) has recently announced a dividend cut of 62.5% due to a strategic transformation that will see the company move toward a long-term strategy of debt reduction, share repurchases, and growth initiatives. While many analysts have commented on the dividend cut as positive for the company, I will take a deeper look at the rationale behind the cut for other long-term Foolish investors.

The transformation

DH Corp. operates in the financials industry. Once a key supplier of paper cheques, the company has transformed itself into largely a financial software and services company. Approximately 40% of the company's revenues now come from its software-as-a-service (SAAS) products with 40% coming from other recurring-transaction financial services; the remaining amount comes from "non-recurring sources."

The appeal of the SAAS business model and other recurring-revenue models is that revenues can be somewhat accurately forecasted due to the nature of the revenues. The vast majority of the company's revenues are contracted for a set period of time, offering the company earnings stability–a big plus for long-term investors looking for relative dividend safety.

The company has grown its recurring-revenue business organically and through acquisitions, which have involved large long-term debt obligations. Let's take a look at these debt obligations further.

Upcoming bond payments

Under note 12 of the company's most recent financial statements, a list of the upcoming bond payments DH is obligated to make outlines further the rationale behind the dividend cut.

We can see that the company paid out $90 million in dividends in 2016, but the company's upcoming bond payment of $80 million is due June 2017. The company has made a decision to pay out this dividend with operating earnings rather than use its credit facility or raise additional debt.

This move is widely considered to be a prudent move for the company long term, especially considering the company's stock price has taking a large hit after missing earnings estimates in late October, This means the new dividend yield (the annualized dividend divided by the current stock price) may still be acceptable for dividend investors who wish to purchase more DH Corp. stock.

Conclusion

The company's dividend-cut announcement last week was greeted with a positive outlook from the market; the stock has appreciated approximately 30% since the announcement. I will maintain a "wait and see" strategy with DH Corp. and reassess how the company distributes value to shareholders over the coming quarters.

The company has indicated that approximately 40% of the proceeds that would have been designated for dividend distributions will be distributed to shareholders via share repurchases. Of course, this all remains to be seen.

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