Investors: Consider Companies With No Dividends

Description

Although the dividend theme has come to dominate the investment landscape over the past five to 10 years, investors may still want to consider companies that choose not to pay dividends.

When a company makes a profit, there are only two things that can be done with it. The first option is to retain the capital to grow the business. The second option is to share the excess capital with investors, either through share buybacks or dividends. A share buyback is not always all that different from a dividend payment. In both cases, the profits are being shared. With dividends, however, the cash payment is much more transparent when compared to a share buyback, which investors don't always realize is happening.

The challenge for growing companies or those in a rapidly changing business is having the ability to sustain the dividend payments over the long term. This results in many companies adopting a share-repurchase plan (when money allows) instead. This leads to fewer shares outstanding and higher earnings per share (EPS) over the long term. In these circumstances, investors must consider if the shares retired were bought back at an appropriate price. Typically, when there is excess cash for a share buyback, shares have already increased in value to reflect the higher than expected profits.

Let's take shares of **CGI Group Inc.** (TSX:GIB.A)(NYSE:GIB) as an example. The company does not pay a dividend, instead opting for a share buyback. At the end of fiscal 2013 (with a year end of September 30), the total number of shares outstanding was 310 million, which has since declined to 304.8 million as of the end of fiscal 2016. Currently halfway through fiscal 2017, the company has continued to reduce the total amount of shares outstanding to slightly less than 297 million.

In spite of the company not paying any dividends, investors have still significantly benefited by being patient. The price return for shares of CGI Group for the past year was 17.5% with a total gain of 175% over the past five years. The compounded annual growth rate (CAGR) over the past five years is nothing short of 28.8%!

For those considering this name, it is important to note that the company is in the business of servicing clients' information technology needs. The business can be compared to a mechanic working at a garage, but instead of working on cars, the company maintains computers and the networks supporting them. Investors can rest assured that the business model is sustainable. Over the past four fiscal years, top-line revenues have risen from $10.08 billion to $10.68 billion. The CAGR in revenues is 1.94%, but the growth in EPS is much higher.

Given the share buyback, the EPS have increased from $2.21 to $3.49 over the same period. This translates to a CAGR of 46.45%! Again, investors have reaped the benefits.

Although not every company chooses to pay dividends, it does not mean that investors should not consider investing in them. There are sometimes overlooked opportunities waiting to be realized.

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