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REMOVAL OF DIVIDEND RESTRICTION

R. VENKATARAMAN

THE REMOVAL of restriction on dividend distribution with effect from 6th July, 1976, is yet another step in the right direction towards the revival of the capital market and improvement of the investment climate in the country. The move has been widely welcomed by stock exchanges and the investors in general. Since the market has been anticipating it from March, a steady undertone of buoyancy ruled in the market for some time.

As the share market price structure has already absorbed this factor, the equity values have not been pushed up very much in the stock exchange deals. However, investment circles expect that, with one big constraint removed, share values will go up and attract greater support from *bona fide* individual investors and institutions. The management of several companies had, in recent months, postponed their decisions regarding dividend payments, waiting for the removal of the restrictions. They are now free to distribute dividends according to the normal company practice and give the shareholders their due. We have no doubt that this will stimulate stock exchange revival and also greater savings and investments in the private corporate sector.

In the wake of the galloping inflation, when the wholesale price index had jumped from 207.1 in 1972-73 to 254.2 in 1973-74 and spiralled higher to 289.1 in May,

308.1 in June and 314.5 in July, 1974, the Government of India promulgated on 6-7-1974, the Companies (Temporary Restrictions on Dividends) Ordinance prohibiting the companies from declaring or paying dividend for any financial year exceeding the "distributable profits for that year", which was defined as one-third of the net profit of the company or the amount required to pay 12% dividend on the face value of equity shares and the dividend payable on the preference shares, whichever was lower. This measure was part of the Government's regulation of money supply and drive against inflation. The period of hyper-inflation in 1973-74 had induced a spurt in equity prices also. The imposition of dividend curbs, aimed mainly at the inflationary situation, also led to a substantial decline in share values after July, 1974. The all-India index number of Security Prices which rose from 103.1 in 1972-73 to 133 in the week ended July 6, 1974, came down to 102.9 by September and went down further to as low as 93.9 in October, 1975. As a result, shareholders incurred losses and potential investors were scared away. The New Issue market also suffered heavily and very often brokers and financial institutions were saddled with a disproportionate percentage of new issues underwritten by them. Many companies had to postpone their plans for expansion and diversifi-

cation and new collaboration agreements had to be deferred. As the yield on equities reached low levels, investable funds moved towards company deposits, which carried interest between 12 to 15 per cent for periods ranging from 1 to 3 years. Thus, the stagnation in the capital market pervaded over a period of two years. The rigours of the Dividend Limitation Act was, however, mitigated with effect from 1975, when declaration of dividends higher than the prescribed limit was permitted on condition that the portion of the dividend in excess of the limits should be paid as deferred dividend in two equal instalments spread over the next two years. This merely increased the paper work for the companies, without making any appreciable impact on the stock exchange.

The Dividend Limitation Act was not, however, without its merits. A steep rise in costs due to various reasons including the high interest rates led to an aggravation of the working capital problems. With the recession in industrial economy, inventories mounted up and the corporate sector was faced with an acute shortage of funds. Unfortunately, this period synchronised with stringent measures of credit control adopted by the banks for the control of inflation. During this period of financial stress, the dividend limitation, by reducing the outflow of funds, enabled some

companies to increase their retained earnings either for adding to their fixed assets or for meeting their working capital needs. In a way the dividend curb helped the management to tide over the monetary stringencies, though the shareholders were adversely affected.

The lifting of the curb by itself cannot create a stock exchange boom. So long as investment in company deposits is more lucrative than investment in equities, the stock market will be dragging its feet and fresh floatations will be severely handicapped. We have adverted earlier to the deleterious effect of high interest rates on the cost of production and on the expansion of sales. This apart, high interest rates are likely to syphon off investable funds from the

equity market and starve new floatations of necessary resources.

One of the reasons why investors prefer equity to deposits is the prospect of capital appreciation. Shareholders expect issue of bonus shares as well as dividends in cash. As an anti-inflationary measure, the Government raised the time lag between two successive bonus issues from 18 months to 24 months. The Companies (Transfer of Profits to Resources) Rules, 1975, issued in September last, lay down several restrictions on the quantum of dividends which can be declared. For instance, no dividend should be paid except after transfer to reserves at a specific percentage of the current profits. Again, compa-

nies are required to maintain on the enlarged capital after issue of bonus shares, a dividend at the average rate on the previous three years. These regulations limit the ability of the company to issue bonus shares. It, therefore, appears unnecessary to continue the present restriction of a 24-month time lag between two bonus issues. The Government has since the last Budget announced several fiscal and other incentives to revive industrial production. Already, there are indications that the growth rate of the industrial sector is picking up well. As the general economic conditions are fast improving, the private corporate sector may be expected to show better results during the current year.

WEST ASIA—THE ARAB-ISRAELI CONFLICT

Mr. K. V. PADMANABHAN
I.F.S. (Retd.)

WITH THE Lebanese crisis showing no signs of abatement — in fact the fighting in Beirut itself has intensified — anxious eyes are turned in the direction of Israel, Lebanon's powerful neighbour in the south. It has been clear for some time that Israeli leaders do not at all like what is happening in Lebanon, but they have so far shown considerable restraint in their comments and action. Now after the latest flare-up, Western correspondents have quoted the Israeli Foreign Minister, Mr. Yigal Allon, as saying that Israel would not tolerate any settlement which would destroy the influence of the Maronite Christians and give a free hand to the Palestinians in Lebanon. Everybody knows that Israel does not make idle threats.

A Cataclysmic Event

Israel is comparatively a newcomer on the West Asian political scene. The modern State of Israel was born on May 14, 1948, in a welter of fighting and chaos. For the Jews it was a dream come true. For the Arabs it was a great betrayal. It will be useful to trace briefly the emergence of this State which has proved to be such a cataclysmic event in the region.

The Jews staked their claim to

Palestine on the ground that they had occupied the region, intermittently, for nearly 1,000 years, before they were driven out by the Romans at the beginning of the Christian era. Since then the Jewish people, who were dispersed all over the world, were sustained by the hope that one day they or their children would be able to return to Zion, the land of their fore-fathers. The Arabs who reject this claim, maintain that the Jews were themselves usurpers and that the original inhabitants of the disputed territory were the Philistines (from whom the name Palestine is derived) and the Cananites. The Arabs sincerely believe that Israel owes its resurrection to the machinations of certain Western Powers, particularly Britain. While there may be some basis for this view, it cannot be denied that the success which the Jews have achieved so far is due to (a) the single-minded devotion to their cause and the wise leadership they were fortunate to have and (b) the disunity and the lack of proper leaders on the side of the Arabs.

The disintegration of the Ottoman Empire during World War I provided an opportunity to the Jewish leaders to press their

claim for the resettlement of their co-religionists in Palestine. In 1916, Britain, as part of her campaign against Turkey, was planning a thrust into the Arab peninsula with a view to cutting the strategic Turkish railway line from Damascus to Medina. To ensure the success of these operations the British opened negotiations with the Arabs. To the Arabs, whose leader was Hussein, the Sheriff of Hejaz, Britain had promised independence if they took up arms against Turkey and cut the railway line to Medina. Hussein and his sons, Abdullah and Feisal, duly completed their part of the bargain with the help and guidance of T. E. Lawrence (the famous Lawrence of Arabia) which enabled General Allenby to advance to Jerusalem and Damascus. But the Arabs were in for a disagreeable surprise.

The Balfour Declaration

What they did not know was that Britain had also been in contact with the Zionists in London for help in the fight against Turkey and had given them an assurance supporting their aspirations for resettlement in Palestine. This was the famous Balfour Declaration of 1919. It was to the effect that the British viewed with favour the establishment in Palestine of a National Home for the Jewish people and will use their best endeavours to facilitate the