Dilution Factor Calculation for Special Dividends

Consultation Paper

31 July 2014

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Invitation to comment

ASX is seeking submissions on this consultation paper by Friday, 12 September 2014. Submissions should be sent to:

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Regulatory & Public Policy ASX Limited
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Attention: John Williams

ASX prefers to receive submissions in electronic form. Submissions not marked as 'confidential' will be made publicly available on ASX's website.

If you would like your submission, or any part of it, to be treated as 'confidential', please indicate this clearly in your submission.

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Introduction

ASX is proposing, following a period of consultation, a change to the methodology utilised by ASX to calculate a dilution factor for special dividends and non-recurring special distributions.

Currently ASX calculates a dilution factor for every special dividend and non-recurring special distribution that is declared. ASX Dilution Factors are published the day before the ex-date. It is proposed that a threshold be introduced that would determine if a dilution factor is calculated.

The proposed change is being considered following feedback from some end users who use ASX Dilution Factors suggesting that a review of the current methodology is required. The suggested threshold is consistent with the practices of other market venues and vendors who provide similar adjustments for special dividends.

ASX is seeking feedback from customers who use ASX Dilution Factors on the implications of the proposed change on their use of the information provided.

ASX is inviting interested parties to consider the proposal and provide comment to ASX by 12 September 2014.

Depending on the feedback received regarding the proposed change, ASX is seeking to implement the proposed change effective 1 November 2014.

Background

A dilution factor is an adjustment figure that is provided by ASX to external subscribers as well as used internally. The objective of diluting per share series data (e.g. Price, Earnings Per Share (EPS), Net Tangible Assets Per share (NTA), Dividend Per Share (DPS) and others…) is to adjust the historical data so it is comparable with current data. A "per share" statistic at one financial reporting period end date may only be correct at that point in time and when viewed from a different capital structure may present a varying statistic. A series of "per share" statistics needs to be adjusted to provide a consistent time series from which meaningful conclusions can be drawn about growth rates, trends and other analytical data. Historical values are not comparable with current values where there has been an intervening pro-rata issue, whether cash or bonus, to existing shareholders. The most common application is in the charting of prices and other time series based data.

The calculated theoretical dilution factor resulting from the corporate action is applied retrospectively to adjust all historical per share values to make them comparable with ex-issue (after the issue) values.

A dilution factor provides a means for data users to compare prices over time on a similarly capitalised company and may be applied by users to historical prices retrospectively from the day before the ex-date to the start of the price records. Dilution factors are calculated for corporate actions such as entitlement issue, special dividend, capital return, reconstructions and others.

Examples of use includes to adjust historical financial per share data such that it is comparable with current data. The rationale for making these adjustments is because a "per share" statistic at a specific point in time will only be correct at that point. When viewed at a later time, where there has been a change in the capital structure, may present misleading statistics.

Further information regarding ASX's Dilution Factor product is included in the product guide.

Current Practice

ASX's current practice is to publish a dilution factor for special dividends that are: one-off, non-recurrent, out of the ordinary course of business, and take the form of a cash or in-specie return or distribution of shares in another entity.

In conjunction with S&P Australia Index Services, ASX introduced the calculation of dilution factors for non-recurring special distributions and special dividends in January 2007. This aligned both entities with what was then global best practice. At the time, ASX received feedback from a number of market stakeholders expressing concerns that these types of distributions/dividends do have a dilutive effect on the market price of the stock and hence have an impact on the portfolio where these particular stocks are a component.

The payment of ordinary dividends by a company has an influence on the price of ordinary shares, with the ex-dividend price expected to fall by the amount of the dividend per share. However, the payment of ordinary dividends does not give rise to a dilution since it is considered to be in the ordinary course of business.

Special dividends are, by their nature, out of the ordinary course of business and take the form of a special cash or in-specie return or distribution of shares in another entity. The term "special dividend" implies a one-off rather than a recurrent payment. As such, it does not give rise to an anticipation of future dividends. Its effect, depending on the size and nature, is to dilute the price of ordinary shares by an amount, which is equal to the value of the dividend or scrip.

ASX Special Dividend Dilution Factor Calculation

A dilution factor for a special dividend dilution is calculated as:

$$\frac{\text{Close Price} - \text{Special Dividend}}{\text{Close Price}} = \text{Dilution factor}$$

Proposed Change

It is proposed that a dilution factor will only be calculated for a special dividend, or other form of cash distribution, where the value of the payment is greater than or equal to 5 per cent of the share's closing price at the time of calculation (the day before the ex-date date). If the value of the special dividend is less than the proposed threshold a dilution factor would not be calculated for that particular event.

The methodologies applied by other listings exchanges and information vendors have been reviewed for similar events to ensure the proposed change is consistent with best practice for the calculation of adjustments.

ASX has consulted with a sample of end users to gain an understanding of how its Dilution Factor Product is used within their processes and calculations. From discussions it was evident that some users may consider an ASX Dilution Factor in their calculations. However, they may also obtain similar adjustments from a range of information vendors, such as Thomson Reuters (Datastream), Bloomberg, or IRESS.

International review

A review was undertaken of market venues and vendors who provide similar calculations to those provided in the ASX Dilution Factor Product and include adjustments for special dividends.

Standard & Poors do not use ASX calculated dilution factors in its calculation and adjustment of S&P/ASX indices.

The table below provides further details.

Market Venue/Vendor	Threshold
National Stock Exchange India	Greater than 10%
Hong Kong Stock Exchange	Greater than or equal to 2%
MSCI	Greater than or equal to 5%
Thomson Reuters	Country specific thresholds apply (examples are: 10% for Australia, 25% for Hong Kong)
LIFFE/ICE	No Adjustment/calculation for Special Dividends

Consultation Questions

You are invited to comment on this proposal. In addition to responding to the consultation, any other feedback relevant to dilution factors is welcome.

Q1 The impact, if any, that a change to the dilution factor methodology described would have on your internal systems and processes; and an indication of the time required to make any necessary changes in response to the proposed change.

Q2 Do you support the proposed changes to ASX's Dilution Factor methodology for special dividends? If so, please outline the key benefits to your organisation.

Q3 Do you support the proposed threshold of greater than or equal to 5 per cent of the share's closing price at the time of calculation?

Q4 What alternative methodologies might be suggested?