Record Stock Buybacks are Seen as Healthy

But there are other ways to enhance shareholder value too

Rewarding shareholders with M&A activity, dividend payouts and stock buybacks, at the expense of capital spending, is very popular in corporate America. You can see its investor appeal as activist groups and talking media heads are continually pushing for these awards.

But this trend could be considered worrisome – dispensing goodies in the present instead of building for the future.

Without question, there is so much to worry about if you are the chief executive officer of a company: revenues are not growing fast enough, you have cut all the expenses you can over the past five to seven years, earnings growth is slowing, and employees – your #1 asset – are hard to find.

What are you to do to enhance shareholder value?

Merge & Acquire

If you are like many companies that have stored up lots of cash, you need to do something with it. Ok, go buy something if you can. Certainly, mergers and acquisitions, which after all is capital spending, appear to be an easier way to grow than expanding internally.

Globally, M&A returned to pre-2008 crisis levels and in the first nine months of 2018, set a record with close to $3.3 trillion in deals – a 39% jump over 2019. Trouble is, many of these deals will fail for reasons ranging from bad strategic fits to cultural clashes between the two companies to plain old bad timing.

If M&A is out, maybe you raise the dividend or do a buyback program.

Raise Your Dividend

More dividends should turn into a higher stock price, right? Purchasing your stock, assuming the same earnings, mathematically dictates that the earnings per share will go up because there are fewer shares to divide up the profits pie. That should increase demand for them and thus the price.

And in 2018, a lot of companies raised their dividends. In fact, according to Standard & Poor's, dividends paid by S&P 500 companies totaled $119.8 billion in the final three months of 2018, setting a quarterly record. And for all of 2018, S&P 500 dividends totaled $456.3 billion, up from $419.8 billion a year ago.

Buyback Your Shares

Like raising a company's dividends, 2018 was a record year for buybacks.

Again, according to Standard & Poor's, in the third quarter of 2018, stock buybacks set a new record of $203.8 billion, which is the third consecutive quarterly record and a 57.7% increase from the $129.2 billion reported for Q3 2017. And when 2018 buyback numbers are finalized, analysts expect the total to be a new annual record north of $1 trillion.

Short-term vs. Long-term

The economic utility of M&A, increased dividends and stock buyback programs, however, is unclear and there is a lot of debate and research about whether each is good or bad.

Advocates note that with companies investing in their own business and with money going back into the "markets," then this causes consumer confidence to rise, consumer consumption to rise, and then stock prices to rise. Well, that's the theory.

Critics on the other hand suggest that these efforts simply result in corporations giving money to their shareholders instead of investing in something more productive and broadly beneficial to their long-term success.

While shareholders may like one or all of these activities in the short run, there will always be long run trade-offs. Because if you are the CEO using your cash to raise your dividend, buy a competitor or buy your own shares, it means you are not using it to expand your business. And in the long run, such expansion might be the better thing for shareholders.

Or it might not.