Diary of a Private Investor CRH Colm Fagan 1 November 2015

A proud tradition can be a source of strength for a family, a community, or even a business, but it can also be a millstone for its custodians. Last year, I decided that CRH, the Irish building materials company, was weighed down by its proud tradition, so I sold my shares. I'm now wondering if it's time to buy some back.

I bought CRH in May 2006 at €27 a share. The dividend for the year was 52 cents, so the dividend yield was under 2%. This was less than I could have earned elsewhere but CRH had a proud tradition of increasing its dividend every year for more than 20 years. I was hoping for more of the same.

Things started promisingly. The dividend for 2007 was increased by over 30%, to 68c a share. It was increased again for 2008, this time by just a single cent, to 69c a share, but by now the recession was approaching its nadir and CRH, as a major player in the construction industry, was suffering. On the very day it announced the higher dividend for 2008, it also asked shareholders for extra money by way of a "rights issue". We thus had the peculiar situation that it was giving money to shareholders with one hand and asking for some back with the other. Why didn't it bite the bullet and cut the dividend? Was it a reluctance to break with the proud tradition?

It was a 2 for 7 rights issue, meaning that I could buy 2 extra shares for every 7 I already held. The cost of each additional share was just €8.40, considerably less than the €15.065 share price ruling at the time. The "special offer" was being funded with our own money, so the price had to fall to €13.58 immediately afterwards. (The numerically minded can check the numbers, based on the fact that every 7 shares I owned beforehand, plus twice €8.40, should be equal in value to the 9 shares I owned immediately afterwards).

Since then, the dividend has been maintained at 62.5c a share. Technically, this is marginally higher than the 69c dividend that applied before the rights issue, so the proud tradition lives on - but at a cost. In 2010 and 2013, CRH had to dip into reserves to pay the dividend as profits in those years were less than the cost of the dividend. There was also some severe cost-cutting during this period.

In April 2014 I decided that CRH's preoccupation with maintaining the dividend was not good for the business. I sold my shares at €21.49. This was less than the €27 they cost me in the first place, but my loss was mitigated, firstly by the dividends received in the meantime, secondly by the profits on the €8.40 rights issue shares, and thirdly by my decision to opt for scrip dividends instead of cash on a number of occasions. Scrip dividends were another device aimed at persuading shareholders to reinvest in the business; for example, instead of taking the October 2013 dividend in cash, when the price was €17.85, I succumbed to the lure of additional shares at the discount price of €15.79.

I was lucky in the timing of my decision to sell: the price fell from €21.49 at which I sold in April 2014 to less than €16 four months later. More recently however, the market has looked more favourably on CRH. One of the main reasons for the market's optimism is that CRH agreed two potentially transformative deals in 2015. The first was a by-product of the merger of two of its competitors, Lafarge of France and Holcim of Switzerland. Competition authorities approved the merger but only on condition that the merged entity sell some of its businesses. CRH bought them, presumably at a knockdown price given the forced nature of the sale. The second potentially transformative deal is the proposed acquisition of a Californian glazing company. The total cost of the two acquisitions is over €7.5 billion - a lot of money in anyone's language. Money for the acquisitions came partly from issuing €1.6 billion worth of shares and the balance from extra borrowings and retained cash.

The share price, now hovering around €25, reflects this newfound optimism. The dividend is still 62.5c a share, so the dividend yield is around 2.5%. A yield this low is only acceptable if there are good prospects for dividends to grow in future. Profits for 2014 were just 78.9c a share, less than 30% more than the cost of the dividend. Assuming that the directors' long-term goal is to pay 50% of profits in dividends and to reinvest the other 50%, profits will have to increase to around €1.30 a share before the dividend can be increased.

Profits of 130c a share may seem a long way from last year's 78.9c, but the recent acquisitions could work wonders for earnings, probably not in 2015 but definitely in 2016 and beyond, when management should be able to realise savings from streamlining the various businesses. Some analysts are forecasting that earnings per share in 2017 will be more than double their 2014 levels.

On the other hand, there are risks - lots of them. One is the high level of debt (around €10 per share) and the associated interest cost. The challenge of integrating the various businesses carries execution risk and operational risk is also higher because CRH is now so much bigger than before.

CRH may no longer be weighed down by its proud tradition, but there are too many unknowns and too many risks for my liking. I have therefore decided to pass for now.