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## How Norwegian Managers View Dividend Policy

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## **How Norwegian Managers View Dividend Policy**

### **Abstract**

We report the results of a 2004 survey from managers of dividend-paying Norwegian firms listed on the Oslo Stock Exchange about their views on dividend policy. Specifically, we identify the most important factors in making dividend policy decisions and managers' views about various dividend-related issues. The most important determinants of a firm's dividend policy are the level of current and expected future earnings, stability of earnings, current degree of financial leverage, and liquidity constraints. No significant correlation exists between the overall rankings of factors influencing dividend policy between Norwegian and U.S. managers. Norwegian managers express mixed views about whether a firm's dividend policy affects firm value. Respondents point to the possible role of dividend policy as a signaling mechanism. No support exists for the tax-preference explanation for paying dividends.

## How Norwegian Managers View Dividend Policy

### 1. Introduction

In his classic work, Black (1976) found no convincing explanation of why companies pay cash dividends to their shareholders. In the three decades since Black first described the “dividend puzzle”, financial economists have intensely studied the possible role of dividends in maintaining or increasing corporate values. According to Baker, Powell, and Veit (2002a, p. 255), “despite a voluminous amount of research, we still do not have all the answers to the dividend puzzle.” That is, we do not have definitive answers on why companies pay dividends and why investors care about them. Nonetheless, theoretical and empirical studies have provided many useful insights about dividend policy. Although the various theories of dividend policy typically take a “one-size-fits-all” approach, evidence suggests that dividend policy may vary substantially from one firm to another. As Frankfurter and Wood (1997, p. 31) conclude, dividend policy “... cannot be modeled mathematically and uniformly for all firms at all times.”

Researchers have followed two major paths in trying to explain why firms pay dividends. The most well traveled path is to develop and test various theories to explain the dividend puzzle. Some of the earliest research focused on the Miller and Modigliani (1961), hereafter called M&M, argument for dividend irrelevance. Based on some highly restrictive assumptions involving perfect capital markets, M&M contend that one dividend policy is as good as another.

Others provide plausible explanations for dividend relevance outside of M&M’s idealized world of economic theory. Common explanations of dividend relevance involve asymmetric information (signaling), taxation, and agency costs.<sup>1</sup> Baker and Wurgler (2004) propose a new explanation called the “catering theory of dividends.” According to this theory, investor preferences for dividends may change over time. Managers cater to investors by paying

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<sup>1</sup> Lease et al. (2000) provide a useful discussion of these dividend theories and research related to them.

dividends when investors place a stock premium on payers, and by not paying when investors prefer non-payers. Each theory has some empirical support but no single theory has emerged as the dominant explanation.

The second path is to survey managers about their views toward possible reasons underlying dividend decisions. Lintner (1956) conducted the seminal study about dividend decisions in the United States. According to Lintner's model, the best predictors of current dividends are past dividends and current profits. He finds that firms have long-term target dividend payout ratios that lead to smoothing of dividend payments over time. His evidence also shows that managers are reluctant both to announce dividend increases that they may later have to reverse and to cut dividends temporarily.

Almost 30 years later, Baker, Farrelly, and Edelman (1985) and Farrelly, Baker, and Edelman (1986) surveyed chief financial officers (CFOs) of NYSE firms from three industry groups (utilities, manufacturing, and wholesale/retail) to identify the major determinants of corporate dividend policy. Their evidence shows that the most important factors are the anticipated level of future earnings, the pattern of past dividends, the availability of cash, and the desire to maintain or increase the stock price. Similar to the findings of Lintner (1956), they report that firms try to avoid changing dividend rates that might soon need to be reversed, maintain an uninterrupted record of dividend payments, have a target payout ratio, and periodically adjust the payout toward the target. Respondents show strong agreement that dividends provide a signaling device and the market uses dividend announcements to help value firm stocks. Finally, they report differences in responses between more regulated (utilities) and less regulated (manufacturing and wholesale/retail) industry groups.

Numerous dividend surveys involving U.S. firms followed including Baker and Farrelly (1988), Farrelly and Baker (1989), Pruitt and Gitman (1991), Baker and Powell (1999, 2000), Baker, Veit, and Powell (2001), and Baker, Powell, and Veit (2002b). Perhaps the most relevant of these surveys are by Baker and Powell (1999, 2000), who update Baker, Farrelly, and

Edelman (1985). Their survey of CFOs from NYSE firms reports most respondents believe that dividend policy affects firm value. Respondents show strong support for the signaling explanation for dividends. Overall, the views of managers about setting dividend payments are surprisingly consistent with Lintner's (1956) findings, especially regarding the concern about continuity of dividends. Unlike Baker, Farrelly, and Edelman (1985), Baker and Powell (2000) report few differences among the responses of managers in different industries. They attribute this finding to changes in the economic and competitive environment for utilities.

Several generalizations emerge from the survey research on dividend policy in the U.S. First, the most important factors influencing dividend policy seem to be relatively stable over time and are similar to those identified by Lintner (1956). These factors relate to earnings and the pattern of past dividends. Second, managers commonly believe that dividend policy affects value and therefore is relevant. Finally, managers seem to favor the signaling explanation for paying dividends over others. The evidence using survey research methodology both complements and provides a check of the purely econometric research on dividends.

The primary purpose of this study is to investigate the views of corporate managers of Norwegian dividend-paying firms listed on the Oslo Stock Exchange about (1) the determinants influencing the dividend policies of their firms and (2) theoretical and empirical issues about dividend policy in general. A secondary purpose is to compare the importance that Norwegian and U.S. managers attached to the factors influencing dividend policy. Although there are numerous dividend surveys involving U.S. firms, this is not the case for Norway. We have purposely chosen to study Norwegian firms' dividend policies relative to those of U.S. firms because of the stark differences in government regulations and tax rates between the two countries. Thus, the main contribution of our study is to provide valuable insights on how managers of Norwegian firms view dividend policy. Such insights can provide a bridge between theory and practice.

The remainder of the paper has the following organization. Section 2 provides a discussion of a few differences between the environments in Norway and the United States. Section 3 presents our research questions and empirical predictions. Section 4 explains our methodology including the sample, survey instrument, testing methodology, and limitations. Section 5 offers our survey results and Section 6 provides a summary and conclusions.

## **2. Different Regulatory and Tax Environments**

Companies operate under different regulatory environments in Norway and the United States. Norway's approach to regulatory standards stems from a centralized government that heavily regulates business in order to ensure stockholders' rights. This approach is evident by government-dominant ownership, which often results in a controlling vote in certain firms and industries. Although large investors such as the government often characterize the market, government regulations of Norwegian shareholders prevent any person from holding more than 10% of the outstanding shares. Thus, laws and regulations influence the process of setting dividend policy. Participation in the stock market by Norwegian citizens has lagged until recently. The standard for corporate governance applying to Norwegian firms, with and without the government as a majority shareholder, is set forth with specific guidelines determined by the Ministry of Trade and Industry and the Ministry of Finance.

The regulatory system in the U.S. differs substantially from that of Norway. The Securities and Exchange Commission (SEC) and the states in which companies are incorporated exert certain controls over publicly traded firms. Firms in the U.S. substantially rely on legal protection of investors provided by various laws and large investors are less prevalent. Thus, an extensive system of rules protects both large and small shareholders. These legal rules support a system of active public participation in the stock market. Shleifer and Vishny (1997) conclude that the legal protection of investors and some form of concentrated ownership are essential elements of a good corporate governance system.

The two countries have vastly different economic and tax policies. Norway has moved to a so-called “dual income tax system” that imposes higher rates on wage income but lower flat rates on all forms of capital income. Norway has lowered rates on capital income because of increasingly global tax competition. The marginal personal income tax and social security contribution rates on gross labor are higher in Norway than in the U.S. In addition, the standard rate for the value added tax (VAT) in Norway during 2005 is 24%. In the U.S., there is no VAT. In 2005, the combined corporate income tax rate was higher in the U.S. (39.3%) than in Norway (28.0%).

The treatment of dividends differs between Norway and the U.S. Norway provides a full dividend tax credit at the shareholder level for part of the underlying corporate profits tax and has a flat individual tax rate of 28% on all capital income.<sup>2</sup> As a result, Norway has the lowest overall dividend tax rate among the 30 Organization for Economic Cooperation and Development (OECD) countries. By contrast, before the passage of the Jobs and Growth Reconciliation Act of 2003, the U.S. had the second highest dividend tax rate in the OECD. The Act reduced both the maximum personal tax rate on dividend income from 38.6% to 15% and the top tax rate on capital gains income from 20% to 15%. Thus, this Act lowered the marginal rate on dividends to that of capital gains, thus reducing but not eliminating the tax problem involving dividends.

### **3. Research Questions and Empirical Predictions**

The study addresses four major research questions.

1. What are the most important factors influencing the dividend policies of dividend-paying Norwegian firms?
2. Does the overall importance of the factors influencing dividend policy differ between Norwegian and U.S. firms?

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<sup>2</sup> For a discussion of tax rates among OECD countries, see <http://www.oecd.org/document>.



3. Do Norwegian managers believe that dividend policy affects firm value?
4. Do Norwegian managers favor the signaling or tax preference theory as an explanation for paying dividends?

Accordingly, we advance hypotheses in response to these questions. The first hypothesis is that the most important factors influencing dividend policy of Norwegian firms relate to earnings. Earnings and the availability of cash provide the basis for paying dividends. For example, Lintner's (1956) behavioral model of dividend policy indicates that changes in dividends depend on past dividends and current profits. Based on their analysis, Benartzi, Michaely, and Thaler (1997, p. 1032) conclude that ". . . Lintner's model of dividends remains the best description of the dividend setting process available." Frankfurter and Wood (2003) also find a positive relation between dividends and current earnings. Although changes in dividends say something about changes in earnings, uncertainty exists about whether dividends serve as a leading or lagging indicator of earnings power.

Past surveys involving U.S. firms by Baker, Farrelly, and Edelman (1985), Pruitt and Gitman (1991), Baker and Powell (2000), and Baker, Veit, and Powell (2001) find that factors relating to earnings are among the most important in determining dividend policy. For example, evidence by Pruitt and Gitman suggests that important influences on the amount of dividends paid are current and past years' profits, the year-to-year variability of earnings, and the growth of earnings. Thus, we expect Norwegian managers to base dividend decisions on those variables found empirically to explain corporate dividend behavior, especially those related to earnings.

The second hypothesis is that significant differences exist in the overall importance managers of Norwegian and U.S. firms attach to factors influencing dividend policy. Although we expect that earnings-related factors rank highly with both Norwegian and U.S. managers, we anticipate that the correlation between the overall rankings of factors is not statistically significant at normal levels. Our rationale for this belief stems from the fact that corporations

operate in different regulatory and tax environments in the two countries. We anticipate that such differences should manifest themselves in the importance that managers attach to various determinants of dividend policy. Specifically, we expect that Norwegian managers, compared to their U.S. counterparts, place greater importance on legal rules and constraints but less concern about affecting the stock price and providing a false signal to investors. We believe that the presence of strict government regulations and ownership reduces the role of dividend policy as a signaling mechanism. Thus, if information asymmetry lessens, the need to use dividends as a signaling device should decline.

Our third hypothesis concerns the theoretical and empirical issue of the relation between dividend policy and value. We expect that Norwegian managers will express significantly positive agreement with the notion that paying dividends affects firm value. Under Miller and Modigliani's (1961) assumptions of perfect capital markets, dividend policy is irrelevant. However, real-world frictions and investor preferences can systematically affect dividend policy and make it a relevant decision variable. Although debate stills exists about dividend relevance, survey evidence by Baker and Powell (1999) and Baker, Powell, and Veit (2001) shows that most of their respondents believe that dividend policy affects firm value. We expect that Norwegian managers hold a similar view.

Our final hypothesis is that Norwegian managers favor signaling over the tax preference explanation for paying dividends. According to Miller and Modigliani's (1961) information content of dividend (signaling) hypothesis, dividend changes trigger stock returns because they convey new information about the firm's future profitability. That is, the use of dividends signals management's confidence in the future. Many others such as Miller and Rock (1985) argue that dividends mitigate information asymmetry between management and shareholders.

Numerous studies document the positive association between dividend changes and stock returns such as Asquith and Mullins (1986), Kalay and Lowenstein (1986), and Nissim and Ziv (2001). Other recent studies including DeAngelo, DeAngelo, and Skinner (1996), Benartzi,

Michael, and Thaler (1997), and Amihud and Li (2004) cast doubt on the hypothesized relation between dividend changes and future earnings. By contrast, other recent studies including Garrett and Priestley (2000) as well as Nissim and Ziv (2001) find evidence that dividend changes provide information about the level of profitability in subsequent years. In addition, survey evidence by Baker and Powell (1999) and Baker, Powell, and Veit (2001) shows that managers of U.S. corporations strongly agree with the signaling explanation for paying dividends.

The tax preference explanation states that since the tax rate on dividends is typically higher than on long-term capital gains, investors prefer retention of cash to dividend payments. Thus, firms should keep dividend payments low if they want to maximize share price. This explanation should not apply in Norway because there is a flat individual tax rate of 28% on all capital income. Thus, we expect Norwegian managers to express stronger agreement to statements involving the signaling versus the tax preference explanation for paying dividends.

#### **4. Methodology and Limitations**

In this section, we discuss the sample, survey instrument, testing methodology, and limitations of this study.

##### **Sample**

The Oslo Stock Exchange is part of NOREX, which is the strategic alliance between the Nordic stock exchanges. The NOREX Alliance is the first stock exchange alliance to implement a joint system for equity trading and harmonize rules and requirements between the exchanges with respect to trading and membership. Members of the NOREX Alliance have adopted the same system for classifying listed companies, called the Global Industry Classification Standard developed by Morgan Stanley Capital International, Inc.

Starting with 166 companies listed on the Oslo Stock Exchange in 2004, we use the following screening criteria to develop our sample. First, we exclude subsidiaries of Norwegian

firms if they have no separate management or headquarters. Second, we eliminate international firms listed on the exchange if management is outside of Norway. Such firms would be subject to rules different from Norwegian regulations regarding dividends and tax-related issues. Third, we require the presence of a physical address in Norway. Fourth, we include firms in which the majority of the board is Norwegian. Finally, we include companies that issued cash dividends in the past based on their 2003 annual reports.

We use these criteria to provide a sample consisting of Norwegian firms that recently paid cash dividends. Using these criteria resulted in 121 firms consisting of a mix of small, medium, and large-sized firms. The small-sized firms are often involved with information technology. The large-sized firms typically represent industrials and commercial banks with state ownership, some of which are a direct result of the Norwegian bank crisis of 1988-1992. Some large industrials, however, have little or no state ownership such as oil companies. The four most common industry classifications -- manufacturing, financial services, information technology, and consulting services -- represent about 66% of the population.

### **Survey Instrument**

We modeled the two-page survey instrument after those developed by Baker, Farrelly, and Edelman (1985) and Farrelly, Baker, and Edelman (1986) and later modified by Baker and Powell (1999, 2000). We made only minor modifications to the previous surveys to permit comparisons with U.S. firms.<sup>3</sup> For example, the Baker and Powell (2000) study contained 20 factors influencing a firm's dividend policy, whereas our study includes 22 determinants. We deleted three of the least important and hence lowest ranked factors and substituted several determinants that we consider relevant given Norway's economic and legal environment.

The survey consists of three parts. Part I contains 22 factors influencing dividend policy, which we refer to later as F1 through F22 to indicate their location in the survey. This part of the

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<sup>3</sup> We used a survey instrument based on other previously pre-tested surveys.

survey asks respondents to indicate the level of importance of each factor in determining their firm's dividend policy using a four-point, equal-interval importance scale where 0 = none, 1 = low, 2 = moderate, and 3 = high. Part II contains six questions about the background of respondents and their firms. Part III of the survey asks the respondents to indicate their level of agreement or disagreement with each of 26 closed-end statements based on a five-point response scale. This equal-interval scale is as follows: -2 = strongly disagree, -1 = disagree, 0 = no opinion, +1 = agree, and +2 = strongly agree. The 26 statements fall within five areas involving (1) investor/shareholder preferences, (2) dividend setting process, (3) dividend policy and value, (4) dividends and signaling, and (5) dividends and taxes. The survey contained a code number to identify the respondents. As an inducement to respond, we offered an executive summary of the results. The Appendix contains a copy of the survey.

During April and May 2004, we mailed a cover letter requesting participation in this study along with a stamped, self-addressed return envelope and the survey instrument to the top financial officer of the 121 firms. The cover letter informed potential respondents that we would report the results in summary form and would not disclose any information involving individual companies. We received 34 surveys of which 33 are usable, giving a response rate of 27.3%.<sup>4</sup> Respondents answered virtually every question.

The responding firms represent various industries of which the most common industry type is manufacturing (33.3%) followed by financial services (15.2%). No other industry group amounts to as much as 10% of the responding firms. We intended to partition firms into financial

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<sup>4</sup> Our response rate is slightly lower than reported in recent dividend policy surveys in the U.S. For example, Baker and Powell (1999 and 2000) report a 32.9% response rate among corporate managers of NYSE firms. Baker, Veit, and Powell (2001) and Baker, Powell, and Veit (2002b) report a 29.8% response rate among NASDAQ managers from dividend-paying firms. These studies involved multiple mailings.

and non-financial firms to test for industry effects, but the sample size precluded our undertaking this analysis.

### **Testing Methodology**

To test our first hypothesis, we used a t-test to determine whether the importance that respondents attach to each of the 22 factors influencing dividend policy differs significantly from zero (no importance) and 1.5 (the theoretical mean of the four-point importance scale). Comparing the mean for each determinant to 1.5 indicates whether the factor is relatively more or less important than average (low/moderate importance). In addition, we used a one-sample chi-square test to determine whether a significant difference exists between an observed number of responses falling in each category and an expected number based on the null hypothesis of no difference. To avoid problems associated with inadequate cell size, we collapsed the four-point importance scale into two categories: none/low importance and moderate/high importance. We tested to determine whether significant differences exist between the observed and expected responses.

To test our second hypothesis, we used the Spearman rank correlation coefficient ( $r_s$ ) to determine whether the factors ranked by Norwegian and U.S. managers differ significantly. Because the number of factors is equal to or greater than 10, we computed the  $t$ -statistic associated with the value of  $r_s$ . We used a two-tailed test because we do not predict the direction of the outcome.

We also used t-tests to test our third and fourth hypotheses. That is, we determined whether the level of agreement/disagreement that respondents attached to each of the 26 issues involving dividend policy differed significantly from zero (no opinion). Where possible, we used the chi-square test to determine the significance of the differences among independent groups.

### **Limitations**

As with any survey, this study has several potential limitations. One drawback is the possibility of non-response bias despite taking the normal precautions to reduce this bias such as by guaranteeing confidentiality and offering a summary of the results to respondents. We used two tests to investigate whether non-response bias might affect our results. First, we used the Wilcoxon sign test to compare the median characteristics of the responding firms (sample) with those of the population. The four characteristics are: (1) total assets, (2) debt ratio (total debt/total assets), (3) market-to-book ratio, and (4) dividend payout ratio. This test computes the differences between the population median and each of the sample values, ranks these differences, and compares them according to the signed differences. Having similar characteristics between these groups would lessen the concern about whether the responding firms are representative of the population. No significant differences exist between the responding firms and the population on any of these characteristics at the 0.05 level.

Next, we used the Spearman rank order correlation coefficient to determine whether an association exists between the rankings of the 12 industry classifications by size in the sample and population and then determine whether  $r_s$  (Spearman's rho) differs from zero only by chance. Given that  $r_s$  is 0.7876 and  $n$  is 12, the associated  $t$ -value is 4.04 with  $df = 10$ , which is significant at the 0.01 level using a one-tailed test. Hence, we reject the null hypothesis and conclude that a significant positive correlation exists between the industry rankings in the population and sample.<sup>5</sup>

Another potential limitation is that our study addresses only some of the interesting dividend policy issues. We limited the scope and hence the length of our survey to increase the response rate and to compare the results with previous dividend studies in the U.S. For example, our study provides information about how dividend policymakers view certain

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<sup>5</sup> The results of the Wilcoxon sign test and the Spearman rank correlation coefficient are available from the authors upon request.

determinants and issues involving dividend policy, but it does not provide information about why the respondents hold these views. This decision to focus on several key areas involving dividend policy entails a tradeoff between comprehensiveness and the response rate. As the length and complexity of practitioner surveys increase, the response rate generally declines, which increases the potential for non-response bias. We believe, however, that justification exists for the tradeoff in this situation.

Finally, the importance of specific factors and the views about dividend policy in general could differ by industry group. Research by Michel (1979) and Baker (1988) among others suggests that a positive relationship exists between industry classification and dividend policy. Baker and Powell (2000) conclude that industry type appears to influence the importance that U.S. managers place on some determinants of dividend policy, but some of these differences have diminished over time. Frankfurter and Wood (2003) find no evidence of a systematic relationship between dividend policy and industrial classification. They suggest that variations in dividend policy by industry might be the sole effect of firm size. Given the small number of responding firms and broad distribution of industry types, we could not partition our sample for purposes of conducting a meaningful analysis of the relationship, if any, between dividend policy and industry classification.

## **5. Empirical Results**

We report the survey results in four sub-sections. First, we examine responses to several questions about the respondents and their firm's dividend policy. Next, we discuss the factors influencing dividend policy for Norwegian firms. Third, we compare the results to those reported by managers of U.S. firms listed on the NYSE and NASDAQ. Finally, we examine the responses to statements about investor/shareholder preferences, dividend setting process, dividend policy and value, dividends and signaling, and dividends and taxes. Tables 1 through 7 report our empirical findings.



## **Background Information**

The survey asks several questions about the characteristics of respondents. The respondent profile supports our belief that knowledgeable individuals answered the survey, which, in turn, lends credibility to our results. For example, most respondents (84.8%) indicated that they are actively involved in determining their firm's dividend policy. Those respondents not directly involved in the dividend setting process are generally in investor relations. In addition, almost all survey respondents hold senior managerial positions. The four most common positions or titles of the respondents are chief financial officer (57.6%), chief executive officer (12.1%), investor relations (11.8%), and finance director (9.1%). No other category amounts to more than 5% of the responses.

The survey also contains several background questions about the firm's existing dividend policy. Table 1 displays the responses to three questions about the administration of dividend policy. As Panel A shows, the most influential person in developing the firm's dividend policy is the chief financial officer (54.5%) followed by the chief executive officer (30.3%). As Panel B indicates, most respondents indicate that their firms (87.9%) formally reexamine dividend policy annually. As Panel C shows, about three-quarters (75.8%) of the responding firms do not have an explicit target payout ratio.

We compared the responses to the three questions in Table 1 to those reported by Baker and Powell (2000) for NYSE firms and by Baker, Veit, and Powell (2001) for NASDAQ firms. For all questions, significant differences at the 0.01 level exist among the three groups of respondents. Based on the chi-square test for independent samples in Panel A, the most influential person in developing the firm's dividend policy differs significantly among the Norwegian, NYSE, and NASDAQ firms. The CFO is most influential for Norwegian firms but the CEO occupies this role for U.S. firms.

Another question concerns the frequency that a firm formally examines its dividend policy. As Panel B shows, the majority of respondents for all three groups say that their firms reexamine dividend policy annually. None of the Norwegian managers report that their firms formally reexamine dividend policy on a quarterly basis compared with 19.2% and 36.7% of responses from NYSE and NASDAQ firms, respectively.

The third question focuses on whether firms have an explicit target payout ratio. As Panel C indicates, a smaller percentage of Norwegian firms (21.2%) report having a target payout ratio compared with NYSE (52.5%) and NASDAQ (50.5%) firms. Although not presented in Table 1, chi-square tests show that the responses differ significantly between Norwegian and NYSE firms ( $\Pi^2 = 11.111$  with  $df = 1$ ) and Norwegian and NASDAQ firms ( $\Pi^2 = 9.710$  with  $df = 1$ ) at the 0.01 level, but not between the NYSE and NASDAQ firms ( $\Pi^2 = 0.153$  with  $df = 1$ ) at the 0.05 level.

What do these findings suggest about the administration of dividend policy in Norway compared with the U.S.? The results show that managers of Norwegian firms reexamine their dividend policies less often and a lower percentage of firms have an explicit target payout ratio. An implication of this evidence is that Norwegian managers, in general, may have greater flexibility in setting their dividend payout than do managers of U.S. firms.

### **Factors Influencing Dividend Policy**

Our first research question is “What are the most important factors influencing the dividend policies of dividend-paying Norwegian firms?” Table 2 presents descriptive statistics showing the importance level of each of the 22 determinants or factors, identified later as F, considered by Norwegian managers in setting their firm’s dividend policy. This table lists the factors based on their weighted mean level of importance. Of particular note is that each factor is of high importance to at least one respondent. Overall, this evidence suggests that the importance respondents attach to various factors influencing dividend policy varies among firms.

That is, the factors influencing dividend policy do not consist of a short list of factors. When asked whether factors beyond the 22 listed in the survey are important in determining a firm's dividend policy, 18.2% of respondents answered "yes."

Because the survey contains a large number of factors, we focus on the five most important determinants of dividend policy (F3, F1, F6, F4, and F14). As the positive t-statistics show, each of these factors is significantly greater than the theoretical mean of 1.5 at the 0.05 level or above using a two-tailed test. In addition, the chi-square tests indicate that the proportion of moderate/high responses differs significantly from the proportion of none/low responses for each factor. About 70% or more of the respondents view each of these factors as of moderate to high importance.<sup>6</sup> We call these factors first-order determinants of payout policy.

Three of the mostly highly ranked determinants involve earnings -- the level of current earnings (F3), the stability of earnings (F1), and the level of expected future earnings (F4). These results support our first hypothesis. For the level of current earnings (F3), the highest ranked factor, about 91% percent of the respondents view this determinant in the moderate to high level of importance. Benartzi, Michaely, and Thaler (1997) report a strong past and concurrent link between earnings and dividend changes. Their evidence suggests that U.S. corporations seem to increase dividends only after they are reasonably sure that they can maintain them at the new level. Thus, the importance that Norwegian managers attach to earnings is not surprising because once firms collect their earnings in the form of cash they can pay dividends.

Another highly rated determinant influencing dividend policy of Norwegian firms is the current degree of financial leverage (F6). The high ranking of this factor suggests that responding managers recognize that a firm's dividend policy affects not only the amount of

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<sup>6</sup> Although not shown in Table 2, additional t-tests indicate that the importance of each of the 22 factors differ significantly from zero (no importance).

funds available to distribute to stockholders as cash dividends but also its capital structure. All else equal, as a firm increases its use of fixed cost financing through debt, preferred stock, and leasing, the company increases its financial risk, earnings volatility, and hence ability to pay dividends. By contrast, the more of its earnings a firm retains, the greater will be the equity component of the capital structure. For our sample of 33 responding firms, the mean debt ratio (total debt to total assets) is 68.5%. The high degree of financial leverage of these firms helps to explain why respondents attach such importance to this factor (F6).

Julio and Ikenberry (2004) offer another potential rationale for the relation between dividends and financial leverage. One possibility is to view dividends and high leverage as substitute corporate governance mechanisms on the theory that both reduce the risk that companies will waste their free cash flow. Thus, dividends and financial leverage can help control management's natural tendency to use excess capital to pursue low-return investments.

The fifth most highly rated determinant influencing dividend policy of Norwegian firms is liquidity constraints such as the availability of cash (F14). Although both the level and stability of earnings are important determinants, firms pay dividends from cash, not earnings based on accrual accounting. Thus, the availability of cash affects a firm's ability to pay cash dividends. Firms are typically unwilling to borrow to pay dividends because borrowing would further increase their degree of financial leverage.

(Insert Table 2 about here)

We conduct chi-square tests to determine whether the distribution of responses (level of importance) for each of the five most highly ranked factors differs significantly from each other. As Table 3 shows, no statistically significant differences at the 0.05 level exist among the five determinants despite their different rankings. Significant differences begin to appear when comparing the first-order determinants of dividend payout to lower ranked factors. For example, F3 and F6 (two of the mostly highly ranked factors) differ significantly from F8 (the sixth highest ranked factor) at the 0.01 and 0.05 level, respectively.

(Insert Table 3 about here)

Of the remaining 17 factors, ten do not differ significantly from the theoretical mean of 1.5 and thus represent factors, on average, of low/moderate importance. These determinants (F2, F5, F8, F9, F10, F11, F12, F20, F21, and F22) in the second cluster cover a wide spectrum of factors ranging from legal rules and constraints (F8) to maintain a given payout ratio (F9). The remaining seven factors (F7, F13, F15, F16, F17, F18, and F19) in the third cluster are significantly lower than the theoretical mean. About 64% to 82% of the respondents view the lowest rated factors as of no or low importance. The chi-square tests show that the proportion of none/low responses differs significantly from that of the moderate/high responses for all but one (F13) of the seven lowest rated determinants. This evidence lends support to the robustness of our findings.

### **Comparing Factors between Norway and the U.S.**

Our second research question is “Does the overall importance of dividend determinants differ between Norwegian and U.S. firms?” The three rightmost columns in Table 2 show the rankings of the factors influencing dividend policy as viewed by managers of firms listed on the Oslo Stock Exchange, NYSE (US1), and NASDAQ (US2). Respondents from all markets rank the same three factors as among the five most important in influencing dividend policy: level of current earnings (F3), stability of earnings (F1), and level of expected future earnings (F4). However, the two other factors ranked among the top five by Norwegian managers -- current degree of financial leverage (F6) and liquidity constraints such as the availability of cash (F14) – are either not included or ranked lower in the U.S. surveys.

Numerous large differences exist between the relative rankings by Norwegian and U.S. managers involving the factors influencing dividend policy. For example, one difference is the importance that U.S. managers attribute to the pattern of past dividends (F2). Managers of NYSE and NASDAQ companies rank this factor 2 of 20 and 1 of 22, respectively, compared

with 11 of 22 by managers of Norwegian firms. A chi-square test shows a highly significant difference in the responses among these three groups of managers ( $IT^2 = 57.6$ ,  $df = 6$ ,  $p = 0.0001$ ). In the U.S., firms often devote resources to maintain a stable dividend payment pattern over time. Apparently, managers of Norwegian firms place less importance on past dividends. An implication of these rankings is that a firm's past dividend decisions may place less of a constraint on current decisions for managers in Norway than in the U.S.

Another key difference involves the importance of legal rules and constraints (F8). Norwegian managers rank this factor 6 of 22 compared with much lower rankings by managers of NYSE (15 of 20) and NASDAQ (12 of 22) firms. A chi-square test shows a highly significant difference in the responses among these three groups ( $IT^2 = 16.55$ ,  $df = 6$ ,  $p = 0.0111$ ). This result is consistent with our expectations that Norwegian managers, compared to their U.S. counterparts, place greater importance on legal rules and constraints. Disparities in ranking may stem from the different regulatory environments in Norway and the U.S. As previously discussed, a centralized government in Norway sets regulatory standards and heavily regulates business in order to ensure stockholders' rights. In the U.S., the regulatory environment fosters widespread shareholder participation, not government domination as is evident in certain Norwegian firms and industries.

A third difference in ranking is the concern about affecting the stock price (F5). As expected, Norwegian managers rank this factor lower (14 of 22) compared with managers of NYSE (3 of 20) and NASDAQ (5 of 22) firms. Based on a chi-square test, the responses among the three groups differ significantly ( $IT^2 = 36.17$ ,  $df = 6$ ,  $p = 0.0001$ ). The relatively high ranking of this factor by U.S. managers suggests that they make the dividend decision with a view toward maintaining or increasing the firm's stock price. Apparently, Norwegian managers do not share this concern about the importance of dividend policy on stock price.

U.S. managers also express a much higher degree of concern that a dividend change may provide a false signal to investors (F19) than do Norwegian managers. Managers of NYSE and NASDAQ firms rate this factor as 4 of 20 and 8 of 22, respectively, compared with 18 of 22 by managers of Norwegian firms. A chi-square test reveals a highly significance difference among the responses of these three groups ( $\chi^2 = 45.60$ ,  $df = 6$ ,  $p = 0.0001$ ). The lesser concern that Norwegian managers express about providing a false signal may stem from a strong regulatory environment and government control.

This rational may also explain the low degree of importance that Norwegian managers attach to the needs of current shareholders (F7), which ranks 21 of 22, compared with 9 of 20 and 9 of 22 for managers of both NYSE and NASDAQ firms, respectively. A chi-square test shows a significant difference in the responses among these three groups ( $\chi^2 = 16.30$ ,  $df = 6$ ,  $p = 0.0122$ ). The relatively low ranking of this factor may result from the government-dominated ownership of some Norwegian firms or the diversity of needs between majority and minority shareholders. Norwegian firms are likely to experience fewer agency problems than are U.S. firms because of concentrated ownership and oversight by the government.

To test our second hypothesis, we calculate the Spearman rank order correlation coefficient to determine the strength of the relationship between the rankings of the factors by Norwegian and U.S. managers. First, we calculate  $r_s$  for the rankings of factors provided by managers of Norwegian and NYSE firms. We make several adjustments to facilitate comparing the results between the current study and Baker and Powell (2000). First, we combine the level of current earnings (F3) and level of expected future earnings (F4) into a single factor as done in the NYSE study and rank this factor. Next, we drop four factors (F6, F10, F20, and F22) contained in the current study but included in the NYSE study. Finally, we rerank the remaining 17 factors. The resulting  $r_s$  of 0.3828 ( $t = 1.60$  with  $df = 15$  and  $p = 0.1304$ ) is not significant at normal levels.

Next, we compare the common factors contained in surveys of managers of Norwegian and NASDAQ firms. We eliminate the desire to conform to the dividend payout ratio of the market as a whole (F16) from our analysis because Baker, Veit, and Powell (2001) do not include this factor in their study. In the current study, F16 is the least important of the 22 factors influencing dividend policy. The  $r_s$  is 0.4316 ( $t = 2.09$  with  $df = 19$  and  $p = 0.0503$ ), which barely misses being significant at the 0.05 level.

Whether the relative importance of dividend determinants differs between managers of Norwegian and U.S. firms depends on whether we focus on specific factors or the overall ranking. As expected, managers of Norwegian and U.S. firms attach similar rankings to earnings as a determinant of dividend policy. Yet, the evidence shows no significant correlation at normal levels between the overall rankings of factors influencing dividend policy between Norwegian and U.S. firms. The correlation of the ranking of factors is stronger between Norwegian and NASDAQ firms compared with Norwegian and NYSE firms. We speculate that this result may relate to the characteristics such as firm size in each market. That is, the characteristics of Norwegian firms in our sample may compare more favorably with NASDAQ firms than they do with NYSE firms.

### **Views about Corporate Dividend Policy**

Tables 4 through 7 provide the respondents' opinions about 26 closed-end statements relating to dividend policy in general. Unlike the previously reported results, these responses do not relate specifically to the respondents' firms. We refer to each statement based on its designation in the survey (A1 through E2). We focus on those statements with responses that differ significantly from zero (no opinion) at the 0.05 or above level. Where appropriate, we compare the results of the current study with those of previous U.S. surveys.

### *Investor/Shareholder Preferences*



Table 4 reports how the respondents view six statements (A1 through A6) relating to investor/shareholder preferences. Based on the t-tests, we reject the null hypothesis that the mean value of A1, A6, A4, and A2 equals zero. A majority of respondents agree with each of the four statements. More than 75% of the respondents agree that investors prefer cash to stock dividends (A1) and a firm should be responsive to the dividend preferences of its shareholders (A6). The response to A6 is noteworthy because the same respondents rank the needs of current shareholders (F7) next to last in importance as a factor influencing the dividend policy of their respective firms. Apparently, a disparity exists between how respondents view this issue for firms in general and for their specific firms.

Respondents generally agree that majority shareholders have different dividend preferences than minority shareholders (A4). As previously discussed, government regulations of Norwegian shareholders prevent any person from holding more than 10% of the outstanding shares and government ownership dominates some firms and industries. Attempting to accommodate different preferences among shareholders complicates the task of setting dividend policy.

Although about 30% express no opinion, respondents, on average, believe that investors prefer cash dividends today to uncertain future price appreciation (A2). This latter view is consistent with the bird-in-the-hand explanation for paying dividends, which asserts that paying higher dividends increases firm value because dividends represent a “sure thing” while share price appreciation in the future is uncertain. By contrast, when asked their views about this statement, Baker, Powell, and Veit (2002) report that only 17.2% of respondents from NASDAQ firms agree. Based on research in the U.S., virtually no empirical support exists for the bird-in-the-hand explanation for paying dividends.<sup>7</sup>

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<sup>7</sup> Miller and Modigliani (1961) call the theory that a high dividend payout ratio will maximize a firm's value the bird-in-the-hand fallacy. Bhattacharya (1979) argues that the reasoning underlying the bird-in-the-

(Insert Table 4 about here)

### *Dividend Setting Process*

Table 5 provides insights about how respondents view the dividend setting process. The responses differ significantly from zero (no opinion) for only 1 of 6 statements. Almost 85% of the respondents agree that a firm should change dividends based on sustainable shifts in earnings (B1). This view is consistent with the high level of importance that respondents, on average, attach to earnings (see F1, F3, and F4 in Table 2) in influencing the dividend policy.

Although not statistically significant at normal levels, the only other statement with which a majority (51.5%) of respondents agree is that a firm should strive to maintain an uninterrupted record of dividend payments (B2). In their surveys of U.S. managers, Baker and Powell (1999) and Baker, Powell, and Veit (2002) report that 74.2% and 95.2% of the respondents from NYSE and NASDAQ companies, respectively, agree with B2. Based on a chi-square test for independent samples, the proportion of responses (level of agreement) for B2 differs significantly among the three groups ( $\chi^2 = 62.34$ ,  $df = 4$ ,  $p = 0.0001$ ).<sup>8</sup> Other chi-square tests show significant differences for B2 between responses of managers of Norwegian and NYSE firms ( $\chi^2 = 14.42$  with  $df = 2$ ) and Norwegian and NASDAQ firms level ( $\chi^2 = 55.3$  with  $df = 2$ ) at the 0.01 level. An implication of these findings is that the respondents from Norwegian firms express much less agreement with maintaining an uninterrupted record of dividend payments than do their U.S. counterparts.

(Insert Table 5 about here)

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hand explanation for dividend relevance is fallacious. Survey research by Baker and Powell (1999) produces mixed results for this explanation of dividend relevance.

<sup>8</sup> To perform the chi-square test and to avoid inadequate cell sizes, we collapse the level of agreement from five categories to three -- strongly agree and agree (-2 and -1), no opinion (0), and agree and strongly agree (+1 and +2).

## *Dividends and Value*

The issue of whether dividend policy affects firm value has puzzled researchers and corporate managers for decades. Research on this issue offers contradictory evidence and advice to corporate managers.<sup>9</sup> Table 6 presents responses to six statements involving dividend policy and value. The responses differ significantly from zero (no opinion) for five of these statements (C2, C3, C4, C5, and C6).

The two statements with the highest level of agreement are a firm should devise its dividend policy to produce maximum value for its shareholders (C3) and an optimal dividend policy strikes a balance between current dividends and future growth that maximizes stock prices (C4). A total of 87.9% and 84.9%, respectively, of the respondents agree with these two statements. The high level of agreement with these statements is not surprising given that the theoretical goal of the firm is to maximize shareholder wealth by maximizing stock price. In fact, not a single respondent disagrees with C3. Baker and Powell (1999) and Baker, Powell, and Veit (2002) find that U.S. managers highly agree with these two statements. In addition, Rappaport (1998) notes that corporate boards nearly universally embrace the goal of maximizing shareholder value. In addition, this goal has become politically correct.

The responses are significantly positive on three other statements: higher and more stable dividends are not fully reflected into higher stock prices because the stock market is not fully efficient (C6); macroeconomic factors are more important in determining stock prices than dividend policy (C5); and the market places greater value on stable dividends than stable payout ratios (C2).

The most direct statement relating to dividends and firm value is a change in a firm's cash dividends affects its value (C1). Although a majority (51.6%) of the respondents agree with

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<sup>9</sup> For a discussion of the impact of dividend policy on firm value, see, for example, Lease et al. (1999) and Frankfurter and Wood (2003).

this statement, the mean of the response distribution does not differ significantly from zero (no opinion). Thus, Norwegian managers seem ambivalent about whether dividend policy matters. The responses to this question about the relation between dividends and firm value are inconsistent with our expectations. Overall, the responses produce mixed results.

By contrast, when asked the same question, the responses of managers of U.S. firms are positive and differ significantly from no opinion. According to Baker and Powell (1999), 74.2% of respondents from NYSE firms agree with C1, while Baker, Powell, and Veit (2002) find that 65.2% of respondents from NASDAQ firms agree. The chi-square test shows that the proportion of responses (level of agreement) for C1 differs significantly among the three groups at the 0.01 level ( $\Pi^2 = 18.39$  with  $df = 4$ ). Significant differences at the 0.05 level also exist between the responses of managers of Norwegian and NYSE firms ( $\Pi^2 = 7.06$  with  $df = 2$ ) as well as between managers of Norwegian and NASDAQ firm ( $\Pi^2 = 7.42$  with  $df = 2$ ). Compared with their U.S. counterparts, respondents from Norwegian firms express much less agreement with the notion that a relation exists between dividend policy and firm value.

(Insert Table 6 about here)

### *Explanations for Paying Dividends*

Although the literature contains numerous theories to explain their pervasive presence, dividends remain one of the thorniest puzzles in corporate finance. We focus on the signaling and tax-preference explanations for paying dividends.<sup>10</sup> According to the signaling explanation, announcements of cash dividends convey valuable information about management's assessment of a firm's future profitability that other means cannot fully communicate. On balance, much empirical evidence supports the view of dividends as a signaling device but recent evidence challenges the signaling theory. According to the tax-preference theory,

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<sup>10</sup> See, for example, Lease et al. (2000) for a summary of research on signaling and tax-related dividends.

investors may favor retention of funds over the payment of dividends because of tax-related reasons. Because the tax effect differs among various types of investors, firms may attract investors if they have dividend policies appropriate to their particular tax circumstances.

Panel A of Table 7 shows the respondents' views on six statements that reflect various aspects of the information content of dividends. The means of all six statements (D1 through D6) are positive but only five statements (D1, D2, D3, D4, and D6) differ significantly from zero (no opinion). There is not a single "strongly disagree" response for any of these six statements. The respondents express the strongest level of agreement (94.0%) with the statement that a firm should adequately disclose to investors its reasons for changing its dividends (D1). Its mean of 1.48 is the highest of any of the 26 statements. Such disclosure helps to improve transparency in the market. The high level of agreement that respondents express is consistent with Norway's strict government regulations and disclosure requirements.

Almost 70% of the respondents agree with the notion that investors generally regard dividend changes as signals about a firm's future prospects (D2). This is the most direct statement involving the signaling explanation for paying dividends. This response contrasts sharply with that provided in Table 2 involving the importance that Norwegian managers attach to the desire to send a favorable signal to current or potential investors (or lenders) (F20). Only 54.6% of the respondents believe that this factor is of moderate to high importance in influencing their firms' dividend policy. In fact, F20 ranks 13 of 22 factors.

The only other statement involving dividends and signaling in which the majority of respondents agree (55.3%) is dividend increases are ambiguous because they can suggest either future growth or a lack of investment opportunities (D6). Although managers can use dividend actions to convey useful information, dividend changes may not be perfect signals. According to Easterbrook (1984), dividend increases may be ambiguous signals unless the market can distinguish between growing firms and disinvesting firms. Apparently, Norwegian managers are aware of this potential ambiguity. Given this awareness, the high level of

agreement that the respondents give to D1 is consistent with reducing any ambiguity involving the meaning that dividend increases may convey.

Although the average response to the remaining three statements (D3, D4, and D5) is significantly positive, the percentage of no opinion responses is high, ranging from 42.4% (D3 and D4) to 60.6% (D5). Only 42.5% of the respondents agree that a firm's stock price generally rises when the firm unexpectedly increases its dividend (D3) and a firm's stock price generally falls when the firm unexpectedly decreases its dividend (D4). Respondents express the lowest level of agreement (30.3%) with the statement that investors generally use dividend announcements as information to help assess a firm's stock value (D5).

Panel B of Table 7 presents the responses on two statements involving the tax-preference explanation of dividends (E1 and E2). Based on the t-tests, the mean of each statement does not differ significantly from zero (no opinion). In fact, the typical response reflects uncertainty with more than 65% of the respondents offering no opinion. Respondents are uncertain about whether investors generally prefer to invest in firms whose dividend policies complement their particular tax circumstances (E2). They are also unsure about whether stocks that pay high (low) dividends attract investors in low (high) tax brackets (E1). Thus, the tax preference explanation for paying dividends garners little support for Norwegian firms.

Surveys of U.S. managers by Baker and Powell (1999) and Baker, Powell, and Veit (2002) provide responses on similar statements involving signaling and tax preferences. Both studies provide strong support for the signaling explanation for paying dividends, but find little or no support for the tax preference explanation. In general, the relative importance that managers of Norwegian and U.S. firms attach to signaling versus tax preferences as an explanation for paying dividends is similar.

Taken as a whole, the evidence supports our hypothesis that Norwegian managers favor signaling over the tax preference explanation for paying dividends. Based on the relatively low ranking of factors related to signaling (F19 and F20) shown in Table 2, Norwegian managers

generally appear to view the role of dividends as signaling device as minimal. When they offer their opinions in general, they point to the possible role of dividend policy as a signaling mechanism.

## **6. Summary and Conclusions**

We survey managers of dividend-paying firms listed on the Oslo Stock Exchange to identify the most important factors in making dividend policy decisions and to learn their views about various dividend-related issues. Where appropriate, we compare the views of managers of Norwegian and U.S. firms. Some findings are consistent with our predictions, but others are surprising. Nonetheless, this survey evidence is still important because it reinforces some earlier findings while not supporting others using a different country and period. The findings of this survey lead to several conclusions about dividend policy.

First, the most important factors influencing the dividend policy of Norwegian firms relate to earnings, specifically the level of current and expected future earnings as well the stability of earnings. Other significant determinants of dividend policy include the current degree of financial leverage and liquidity constraints. Based on our evidence, we conclude that the same factors influencing dividend decisions are not equally important to all firms. We surmise that no universal set of factors applies equally to all firms.

Second, the relative importance that managers of Norwegian firms attach to earnings in influencing dividend policy is similar to that previously reported by managers of U.S. firms. However, distinct differences exist in the importance that managers attach to numerous factors. For example, managers of Norwegian firms view legal rules and constraints as more important than do their U.S. counterparts. By contrast, managers of U.S. firms rank the pattern of past dividends as more important than do managers of Norwegian firms. No significant correlation exists between the rankings of factors by managers of Norwegian and NYSE or NASDAQ firms.

Third, Norwegian managers generally support some statements related to the concept that a firm's dividend policy matters. They show a high level of agreement that a firm should devise its dividend policy to produce maximum value for its shareholders. In addition, they agree that an optimal dividend policy strikes a balance between current dividends and future growth that maximizes stock price. Yet, these managers appear ambivalent when asked whether a change in a firm's cash dividends affects its value. Compared with their U.S. counterparts, respondents from Norwegian firms express much less agreement with the notion that a relation exists between dividend policy and firm value.

Finally, managers of Norwegian firms express stronger support for a signaling explanation for paying dividends than they do for a tax-preference explanation. Yet, the majority of responses appear ambivalent to whether investors generally use dividend announcements as information to help assess a firm's stock value. For firms in general, the evidence suggests that dividend policy plays a possible role as a signaling mechanism.



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**Table 1. Administration of Dividend Policy**

This table presents the responses to questions about the administration of dividend policy. Panel A identifies the person who is most influential in developing corporate dividend policy. Panel B indicates how often firms re-examine their dividend policies. Panel C shows the proportion of firms that have target payout ratios. Conducting the chi-square tests required collapsing the responses into the two classes: annual and quarterly/other in Panel B and yes and no/don't know in Panel C. The chi-square tests show significant differences between the responses of Norwegian and U.S. respondents.

Question	Norway (n = 33)	US1 NYSE <sup>a</sup> (n = 198)	US2 NASDAQ <sup>b</sup> (n = 188)	$\chi^2$ stat
<b>Panel A.</b> <i>Who is most influential in developing the dividend policy ultimately approved by your board of directors?</i>				
Chief Financial Officer (CFO)	54.5%	43.9%	25.5%	31.432**  (df = 4)
Chief Executive Office (CEO)	30.3	47.5	66.5	
Other	15.2	8.6	8.0	
<b>Panel B.</b> <i>How often does your firm formally reexamine its dividend policy?</i>				
Quarterly	0.0	18.2	36.7	15.976**  (df = 2)
Annually	87.9	73.7	59.0	
Other	12.1	8.1	4.3	
<b>Panel C.</b> <i>Does your firm have an explicit target payout ratio (a long-term desired dividend-to-earnings ratio)?</i>				
Yes	21.2	52.5	50.5	11.3519**  (df = 2)
No	75.8	46.0	48.9	
Don't know	3.0	1.5	0.5	

<sup>a</sup>Baker and Powell (2000, p. 39).

<sup>b</sup>Baker, Veit, and Powell (2001, p. 31).

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.

**Table 2. Factors Influencing Dividend Policy**

This table presents descriptive statistics showing the level of importance of 22 factors considered by managers of Norwegian firms in setting their firms' dividend policies. The table lists the determinants according to the overall ranking from the highest to lowest mean. The t-statistic indicates whether the mean is statistically different from 1.5 (the theoretical mean of the importance scale). The chi-square statistic indicates whether the combined none/low responses differ significantly from the combined moderate/high responses. The rightmost columns contain the ranking of factors considered by managers of U.S. corporations listed on the NYSE (US1) and NASDAQ (US2) in setting their firms' dividend policies as reported by Baker and Powell (2000, 2001), respectively.

Factor <sup>a</sup>	Level of Importance <sup>b</sup> (%)				Mean (Std Dev)	t- stat	$\chi^2$ stat	Rank		
	None 0	Low 1	Mod 2	High 3				Nor	US1	US2
F3. Level of current earnings	3.0	6.1	48.5	42.4	2.30 (0.728)	6.335**	22.091**	1	1 <sup>c</sup>	3
F1. Stability of earnings	3.0	18.2	42.4	36.4	2.12 (0.820)	4.352**	10.939**	2	5	2
F6. Current degree of financial leverage	9.1	12.1	48.5	30.3	2.00 (0.901)	3.187**	10.939**	3	NA	10
F4. Level of expected future earnings	9.1	18.2	45.5	27.3	1.91 (0.914)	2.571*	6.818**	4.5	1 <sup>c</sup>	4
F14. Liquidity constraints such as the availability of cash	12.1	18.2	36.4	33.3	1.91 (1.011)	2.324*	5.121*	4.5	7	14
F8. Legal rules and constraints	18.2	27.3	21.2	33.3	1.70 (1.132)	1.000	0.273	6	15	12
F11. Expected rate of return on the firm's assets	12.1	33.3	36.4	18.2	1.61 (0.933)	0.653	0.273	7	12	11
F12. Concern about maintaining a target capital structure	12.1	21.2	63.6	3.0	1.58 (0.751)	0.579	3.667	8.5	10	6
F22. Investment considerations such as the availability of profitable investments	12.1	39.4	27.3	21.2	1.58 (0.969)	0.449	0.030	8.5	6	15
F10. Availability of alternative sources of capital	9.4	43.8	28.1	18.8	1.56 (0.914)	0.387	0.125	10	NA	17
F2. Pattern of past dividends	15.2	30.3	39.4	15.2	1.55 (0.938)	0.278	0.273	11	2	1
F21. Financing considerations such as the cost of raising external funds (debt or equity)	6.1	51.5	33.3	9.1	1.45 (0.754)	-0.346	0.758	12	11	19
F20. Desire to send a favorable signal to current or potential investors (or lenders)	18.2	27.3	48.5	6.1	1.42 (0.867)	-0.502	0.273	13	NA	16
F5. Concern about affecting the stock price	18.2	42.4	30.3	9.1	1.30 (0.883)	-1.281	1.485	14	3	5

**Table 2. Factors Influencing Dividend Policy (Continued)**

Factor	Level of Importance (%)				Mean (Std Dev)	t- stat	$\sigma^2$ stat	Rank		
	None 0	Low 1	Mod 2	High 3				Nor	US1	US2
F9. Desire to maintain a given payout ratio	24.2	39.4	27.3	9.1	1.21 (0.927)	-1.783	2.455	15.5	8	7
F13. Projections about the future state of the economy	18.2	45.5	33.3	3.0	1.21 (0.781)	-2.118*	2.455	15.5	17	18
F15. Desire to conform to the industry's dividend payout ratio	18.2	57.6	18.2	6.1	1.12 (0.781)	-2.786**	8.758**	17	13	13
F19. Concern that a dividend change may provide a false signal to investors	15.2	66.7	12.1	6.1	1.09 (0.723)	-3.250**	13.364**	18	4	8
F17. Contractual constraints such as dividend restrictions in debt contracts	39.4	30.3	24.2	6.1	0.97 (0.951)	-3.202**	5.121*	19	14	21
F18. Preference to pay dividends instead of undertaking risky reinvestments	30.3	48.5	18.2	3.0	0.94 (0.788)	-4.086**	10.939**	20	18	20
F7. Needs of current shareholders	33.3	48.5	12.1	6.1	0.91 (0.843)	-4.028**	13.364**	21	9	9
F16. Desire to conform to the dividend payout ratio of the market as a whole	30.3	51.5	15.2	3.0	0.91 (0.765)	-4.437**	13.364**	22	NA	NA

<sup>a</sup> Other factors examined in Baker and Powell (2001), but not included in Table 2 and the current survey, are characteristics of current shareholders such as their tax positions (rank 16 of 20); prestige associated with paying dividends (rank 19 or 20); and control issues such as the firm's ownership structure (rank 20 of 20). Baker and Powell (2000) include stockholder characteristics (e.g. the stockholders marginal tax rates) (rank 22 of 22).

<sup>b</sup> The total number of responses for all factors is 33, except 32 for F10.

<sup>c</sup> Baker and Powell (2000) combine these two factors into a single factor called the level of current and expected future earnings.

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.

**Table 3. Difference in Importance between the Top-Ranked Factors Influencing Dividend Policy**

This table shows the results of the chi-square tests, which indicate whether a statistically significant difference exists between the distributions (level of importance) of each pair of high-ranked factors (F3, F1, F6, F4, and F14). The remaining factor, legal rules and constraints (F8), is the most highly ranked factor that is not statistically different from 1.5 (the theoretical mean). To perform the chi-square tests required collapsing the cells for level of importance from four categories to three categories: none/low (0 and 1), moderate (2), and high (3). Each chi-square test of significance has two degrees of freedom.

Factor	Chi-Square Value				
	F1	F6	F4	F14	F8
F3. Level of current earnings	1.89	2.27	4.12	4.70	11.88**
F1. Stability of earnings		0.32	0.71	0.73	5.29
F6. Current degree of financial Leverage			0.33	1.15	6.48*
F4. Level of expected future earnings				1.15	4.61
F14. Liquidity constraints such as the availability of cash					2.32

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.

**Table 4. Views about Investor/Shareholder Preferences**

This table presents descriptive statistics reflecting the respondents' opinions on six statements related to investor/shareholder preferences (A1 to A6). The null hypothesis is that the mean does not differ significantly from zero (no opinion). The number of responses is 33 for each statement.

Statement	Level of Agreement (%)					Mean (Std Dev)	t-stat
	Strongly Disagree -2	Disagree -1	No Opinion 0	Agree +1	Strongly Agree +2		
A1. Investors prefer cash to stock dividends.	0.0	6.1	18.2	42.4	33.3	1.03 (0.883)	6.700**
A6. A firm should be responsive to the dividend preferences of its shareholders.	3.0	9.1	9.1	57.6	21.2	0.85 (0.972)	5.014**
A4. Majority shareholders have different dividend preferences than minority shareholders.	3.0	18.2	27.3	36.4	15.2	0.42 (1.062)	2.296*
A2. Investors prefer cash dividends today to uncertain future price appreciation.	3.0	15.2	30.3	45.5	6.1	0.36 (0.929)	2.248*
A5. If investors perceive the stock market as displaying unsatisfactory transparency and disclosure practices, the dividend should be higher to attract investors and sustain prices.	3.0	24.2	27.3	36.4	9.1	0.24 (1.032)	1.350
A3. Inside shareholders have different dividend preferences than outside shareholders.	9.1	21.2	36.4	24.2	9.1	0.03 (1.104)	0.158

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.



**Table 5. Views about the Dividend Setting Process**

This table presents descriptive statistics reflecting the respondents' opinions on six statements related to the dividend setting process (B1 to B6). The null hypothesis is that the mean does not differ significantly from zero (no opinion). The number of responses is 33 for all statements.

Statement	Level of Agreement (%)					Mean (Std Dev)	t-stat
	Strongly Disagree -2	Disagree -1	No Opinion 0	Agree +1	Strongly Agree +2		
B1. A firm should change dividends based on sustainable shifts in earnings.	3.0	3.0	9.1	54.5	30.3	1.06 (0.899)	6.775**
B2. A firm should strive to maintain an uninterrupted record of dividend payments.	0.0	27.3	21.2	42.4	9.1	0.33 (0.990)	1.935
B6. A firm should avoid increasing its regular dividend if it expects to reverse the dividend decision in a year or so.	6.1	18.2	27.3	36.4	12.1	0.30 (1.104)	1.577
B4. A firm should view cash dividends as a residual after funding desired investments from earnings.	12.1	18.2	27.3	30.3	12.1	0.12 (1.219)	0.571
B5. A firm should set a target dividend payout ratio and periodically adjust its current payout toward the target.	9.1	18.2	39.4	30.3	3.0	0.00 (1.000)	0.000
B3. A firm should have a dividend policy similar to other listed firms in the same industry.	3.0	33.3	30.3	33.3	0.0	-0.06 (0.899)	-0.387

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.

**Table 6. Views about Dividend Policy and Value**

This table presents descriptive statistics reflecting the respondents' opinions on six statements related to dividend policy and value (C1 to C6). The t-statistics test the null hypothesis that the mean does not differ significantly from zero (no opinion). The number of responses is 33 for all statements.

Statement	Level of Agreement (%)					Mean (Std Dev)	t-stat
	Strongly Disagree -2	Disagree -1	No Opinion 0	Agree +1	Strongly Agree +2		
<b>Dividend Policy and Value</b>							
C3. A firm should devise its dividend policy to produce maximum value for its shareholders.	0.0	0.0	12.1	45.5	42.4	1.30 (0.684)	10.944**
C4. An optimal dividend policy strikes a balance between current dividends and future growth that maximizes stock price.	0.0	3.0	12.1	36.4	48.5	1.30 (0.810)	9.247**
C6. Higher and more stable dividends are not fully reflected into higher stock prices because the stock market is not fully efficient.	0.0	3.0	33.3	54.5	9.1	0.70 (0.684)	5.854**
C5. Macroeconomic factors are more important in determining stock prices than dividend policy.	6.1	12.1	18.2	42.4	21.2	0.61 (1.144)	3.043**
C2. The market places greater value on stable dividends than stable payout ratios.	0.0	12.1	45.5	42.4	0.0	0.30 (0.684)	2.545*
C1. A change in a firm's cash dividends affects its value.	12.1	15.2	21.2	45.5	6.1	0.18 (1.158)	0.902

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.

**Table 7. Explanations of Dividend Policy: Signaling and Tax Preferences**

This table presents descriptive statistics reflecting the respondents' opinions on two common explanations for paying dividends – signaling (D1 to D6) and tax preferences (E1 and E2). The null hypothesis is that the mean does not differ significantly from zero (no opinion). The number of responses is 33 for all statements except D6, which has 32 responses.

Statement	Level of Agreement (%)					Mean (Std Dev)	t-stat
	Strongly Disagree -2	Disagree -1	No Opinion 0	Agree +1	Strongly Agree +2		
<b>Panel A. Dividends and Signaling</b>							
D1. A firm should adequately disclose to investors its reasons for changing its dividends.	0.0%	3.0%	3.0%	36.4%	57.6%	1.48 (0.712)	11.973**
D2. Investors generally regard dividend changes as signals about a firm's future prospects.	0.0%	12.1%	18.2%	57.6%	12.1%	0.70 (0.847)	4.726**
D6. Dividend increases are ambiguous because they can suggest either future growth or a lack of investment opportunities.	0.0%	12.5%	31.3%	43.8%	12.5%	0.56 (0.878)	3.626**
D3. A firm's stock price generally rises when the firm unexpectedly increases its dividend.	0.0%	15.2%	42.4%	36.4%	6.1%	0.33 (0.816)	2.345*
D4. A firm's stock price generally falls when the firm unexpectedly decreases its dividend.	0.0%	15.2%	42.4%	36.4%	6.1%	0.33 (0.816)	2.345*
D5. Investors generally use dividend announcements as information to help assess a firm's stock value.	0.0%	9.1%	60.6%	30.3%	0.0%	0.21 (0.600)	2.031
<b>Panel B. Dividends and Taxes</b>							
E2. Investors generally prefer to invest in firms whose dividend policies complement their particular tax circumstances.	0.0%	9.1%	66.7%	24.2%	0.0%	0.15 (0.566)	1.538
E1. Stocks that pay high (low) dividends attract investors in low (high) tax brackets.	3.0%	12.1%	69.7%	12.1%	3.0%	0.00 (0.707)	0.000

\*\*\* Significant at the 0.05 and 0.01 levels, respectively.



### III. ISSUES INVOLVING CORPORATE DIVIDEND POLICY

**Directions:** Circle the number corresponding to your level of agreement or disagreement with each statement about **dividend policy in general**.

	Level of Agreement					Circle One	
	Strongly Disagree -2	Disagree -1	No Opinion 0	Agree +1	Strongly Agree +2	Level of Agreement Disagree	Agree
<b>A. Investor/Shareholder Preferences</b>							
1.						-2	-1 0 +1 +2
2.						-2	-1 0 +1 +2
3.						-2	-1 0 +1 +2
4.						-2	-1 0 +1 +2
5.						-2	-1 0 +1 +2
6.						-2	-1 0 +1 +2
<b>B. Dividend Setting Process</b>							
1.						-2	-1 0 +1 +2
2.						-2	-1 0 +1 +2
3.						-2	-1 0 +1 +2
4.						-2	-1 0 +1 +2
5.						-2	-1 0 +1 +2
6.						-2	-1 0 +1 +2
<b>C. Dividend Policy and Value</b>							
1.						-2	-1 0 +1 +2
2.						-2	-1 0 +1 +2
3.						-2	-1 0 +1 +2
4.						-2	-1 0 +1 +2
5.						-2	-1 0 +1 +2
6.						-2	-1 0 +1 +2
<b>D. Dividends and Signaling</b>							
1.						-2	-1 0 +1 +2
2.						-2	-1 0 +1 +2
3.						-2	-1 0 +1 +2
4.						-2	-1 0 +1 +2
5.						-2	-1 0 +1 +2
6.						-2	-1 0 +1 +2
<b>E. Dividends and Taxes</b>							
1.						-2	-1 0 +1 +2
2.						-2	-1 0 +1 +2

If you want a summary of the findings, indicate your e-mail address: \_\_\_\_\_

**Please check to see that you answered each question. Thank you for your help.**