

An International Survey of Corporate Financial Behavior by Sector

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Abstract

This survey-based research deals with sectorial differences in terms of three main corporate finance policies: investment, financing and dividend. We used a multinational survey that was distributed to CFOs in five countries: US, UK, Germany, Canada and Japan. We found statistically significant **differences** between the nine sectors examined in terms of all the three major financial policies. These **differences** may be due to: (1) the unique financial needs and operational conditions of each sector, and (2) the imitation effect according to which, firms imitate the financial behavior of other firms in their sector. We found that the use of well-known investment appraisal techniques is most common in the construction sector and least common in the technology sector. The IRR is the most frequently used investment appraisal technique for the entire survey sample, especially in the communication sector and rarely in the technology sector. The lowest financial leverage has been found in the technology sector while the highest was found in the finance sector. A constant sum per-share is the most common dividend policy in the following sectors: retail and wholesale, services, manufacturing and transport. On the other hand, the construction, energy, communication and technology sectors, are characterized by a high percentage of firms that do not pay dividends at all.

JEL Classifications: G3, G32, G35

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.Introduction 1

Studies utilizing questionnaires for examining corporate finance in practice have focused on the financial behavior of companies in a number of countries (Graham and Harvey (2001), Brounen, Jong and Koedijk (2004), and Cohen and Yagil (2008)). Although valuable information has been obtained through these studies, **limited** attention has been given to the potential differences between industries (sectors) ¹.

The present study, therefore, will examine whether, in addition to national differences, there are also sectorial differences in corporate finance practices. The literature on financial economics refers to industry effects in different contexts. For example, each industry or sector has its own business risk and financial risk. Furthermore, financial theory has established that a negative relationship between these two types of risk should exist. In other words, the greater the business risk in a given industry, the lower its financial risk (financial leverage).

The industry effect on corporate financial decisions has been thoroughly discussed in the financial literature. Harris and Raviv (1991) noted that firms in a given industry have similar leverage ratios, while leverage ratios vary across industries. Other studies such as those by Schwartz and Aronson (1967) and Long and Malitz (1985) have found that specific industries share a common leverage ratio that is relatively stable over time. **Beattie et al. (2006) have found little evidence that companies within particular stock exchange sector adopt similar financial strategies. In spite of that, they found in their UK survey that resource companies' respondents agreed strongly that gearing (financial leverage) would be lower for R&D dependent firms than utility firms, and that utilities and resource sectors have greater concern about future cash flows than in information technology and consumer goods. They suggested that current gearing levels could explain different concern about future cash flow.** Myers (1977) argued that equity financed industries tend to have few tangible assets and numerous intangible assets. Rajan and Zingales (1998) identified the industry needs for external finance and examined whether industries that **require substantial external funding** grow relatively faster in developed countries than in undeveloped countries. Their hypothesis implies that industries such as drugs and pharmaceuticals, which require

substantial external funding, should grow relatively faster than tobacco, which requires little external finance. Miao (2005) found that the following industries have relatively low financial leverage (a) high-tech industries (b) industries with high bankruptcy costs, and (c) industries with high fixed operating costs.

Studies suggest that firms pursue a target debt ratio (Taggart (1977) and Jalilvand and Harris (1984)). Campbell (1988) found that the market reactions to changes in the financial leverages were related to whether the change moved the firm closer to or away from the industry average. Hull (1999) found that companies that have drifted away from the common sectorial capital structure have achieved a negative average yearly access return of 3.41%, while companies that approached the common sectorial capital structure have achieved a positive yearly average access return of 1.91%. The researcher's conclusion was that drifting away from the common capital structure has a stronger impact on the stocks' return than approaching it.

Given that differences between sectors may exist in terms of, for instance, the business risk, certain firms may simply imitate the industry corporate policy. Another type of imitation is that of corporate policies of companies that belong to a certain financial index such as the Dow Jones Industrial Average (DJIA). The corporate policies for a company included in such an index can deviate from the typical policies prevailing in the relevant industry.

As far as we know prior questionnaires-based studies have not focused on a comparative analysis of sectorial differences in an international perspective. Country differences have already been examined in prior studies (e.g; Cohen and Yagil (2008)). The present study, therefore, will examine whether beyond country differences, sectorial differences also exist. **It should be emphasized that the sector effects documented in the current paper are not intended to pick up country effects.**

Employing questionnaires sent to CFOs of five countries - US, UK, Germany, Canada and Japan, we found certain sectorial differences with respect to the three types of corporate policies: investment, financing and dividend. For instance, investment appraisal techniques are more common in the construction sector than in the technology sector. Also, long-term debt financing is more frequent in transportation and energy sectors than

in the technology sector. With regard to the dividend policy, the banking and finance is the only sector in which the preferred dividend policy is a constant percent of net income. **Differences between sectors can stem from the following two possible reasons: (1) different industry characteristics (e.g, different growth rates and risk levels) and (2) the different nature of the industry (e.g, the construction and banking industries traditionally rely more on debt than does the technology sector).** This paper will attempt to explain the reasons for different sectorial financial variables. The findings in this paper may help practitioners to widen their understanding of the reasons behind observed financial behavior, and may enable scholars to future examine further whether the financial behavior observed is consistent with corporate finance theory. The plan of this paper is as follows: Section 2 briefly summarizes the relevant literature; Section 3 outlines the methodology and sample; Section 4 discusses the empirical results; and the last section provides a summary and conclusions.

2. Literature Review

Variance in sectorial dividend policies was first predicted by [Lintner \(1953\)](#). He had hypothesized that dividend policy is influenced by the industry effect, rather than the firm specific variables. Dhanani (2005) found that financial and utility firms in the U.K place more value on dividend relevance than their counterparts in other industries do. In his view, these results are related to the enhanced importance that these firms attach to the signaling implications of dividend policy.

Other researches have based their results on managers' surveys but have not focused on sectorial issues. Graham and Harvey (hereafter GH (2001)) found a rise in the frequency of use of the NPV (Net Present Value) as an investment appraisal technique over other questionnaire-based studies cited in their paper. They were surprised by the fact that more than half of the respondents used the company's cost of capital for investment appraisal of an international project, even though the risk in a particular project was likely to differ from the firm's overall risk. Brounen, Jong and Koedijk (hereafter BJK (2004)) have found that while large firms use the NPV and the capital assets pricing model when assessing the financial feasibility of an investment, small firms still rely on the pay back

criterion. In our international survey, we will examine the sectorial differences in the use of known criteria for investment appraisal.

With regard to the financing policy, Modigliani and Miller (1958, 1963) laid the groundwork for future discussions about whether the tax benefits of debt affect financing decisions. GH concluded that the tax benefits of debt (in addition to financial flexibility, bond rating, and profit fluctuation) are the most significant factors shaping the company financing policy. Moreover, they found that bond rating and financial flexibility are the primary factors influencing bond-issue policy, while per share profit, dilution effect and share price on the stock exchange are the primary factors influencing decisions regarding stock issues. BJK too have concluded that financial flexibility is the most important factor determining the firm's target capital structure. The **pecking order theory of capital structure (e.g, Myers (1984)) states that the sources of financing that firms prefer to fund investments follow the following order: retained earnings, debt, and common equity.** We will examine to what extent each sector relies on different sources of financing.

There is a debate in the financial literature regarding the degree to which dividend policy affects company value. Modigliani and Miller (1958) claim that under perfect capital market conditions, a firm's value depends on its operating profitability rather than on whether it distributes its profits. Other researchers reach the opposite conclusion. Kalay and Michaely (2000), for example, claim that dividend policy has a positive impact on long-term stock returns. Baker and Powell (1999) find support for managerial beliefs about the relationship between dividend policy and the firm's value. Moreover, the respondents in their questionnaire study are very much concerned about the continuity of dividends and the signaling effect that dividend changes have. In keeping with Lintner's (1956) prediction, Brav, Graham and Michaely (2005) argue that the perception of stability in future earnings affects dividend policy. They also find that the link between dividends and earnings has weakened over time. More managers now favor stock repurchases because they are viewed as more flexible than dividends and can be used to time the equity market or to increase the earnings per share. Allen (1992) argued that the dominant factors that influence target dividend payouts are maintaining a stable dividend, the company's recent dividend history and signaling considerations. Kumar and Lee (2001) claimed that dividend smoothing ² is intended to attract investors to companies in

financial distress. Li and Lie (2006) argued that the decision to change the dividend and the magnitude of the change depend on the premium that the capital market places on dividends. In their view, the capital market rewards managers for considering investors' demand for dividends when making decisions about the level of dividends. Fama and French (2001) pointed to a drop in the number of companies paying out cash dividends, from 66.5% in 1978 to 20.8% in 1999. This drop, they believe, is the result of the change in the nature of companies traded on the American capital market. There has been a significant increase in the number of small companies traded on the stock exchange that operate with a small profit margin but offer significant growth opportunities.

In our study, we examine the major factors influencing the financing and dividend policies in different sectors. In addition, we describe how managers in different sectors perceive the importance of the three main financial policies: investment, financing and dividend.

3. Methodology and Sample

In order to test the relationship between theory and practice in terms of corporate decisions, two major research methods are generally utilized in the experimental literature³. One method is to rely upon market data and financial statements, while the other is to distribute questionnaires directly to financial decision makers. Each of these two methods has some advantages and disadvantages. The main advantages of the questionnaire method are: (a) Questionnaires make it possible to get information “from the source” that is harder to obtain by alternative methods. For example, the intentions upon which decisions are based can be detected more directly by a questionnaire; (b) A manager’s perspective does not always completely correspond to the financial situation reflected in the raw data. However, as a research tool, questionnaires also have several limitations. Discrepancies occur as a result of partial or tendentious responses or inadequate understanding of the questions asked. Another problem associated with the questionnaire method is the possible lack of reliability and validity. Wallace and Mellor (1988) have suggested addressing the problem of “no response” by comparing late arriving questionnaires to those that arrived on time. Following their recommendation, we compared the mean responses to key questions in surveys that arrived after the three

months requested period with those that arrived on time. We found no statistically significant differences between answers on the early and late questionnaires.

The questionnaire, briefly discussed later in this section, was sent to chief financial officers (CFOs) of major companies in five countries: the US, the UK, Germany, Canada and Japan. These countries were chosen because they had the highest GDP (Gross Domestic Product) per capita among the OECD countries at the time the questions were asked. The companies were selected using leading stock indexes in each country: TOPIX500 in Japan, S&P500 in the US, FT500 in the UK, DAX and MDAX in Germany and TG1000 in Canada. For each country we selected the 300 largest companies included in the index. The number of responding companies ranged between 21 and 35 for each of the five countries (140 in total), resulting in an average response rate of 9.3%. The response rate ranged between 7% and 10% across the five countries in the sample. This rate is similar to the mean response rate obtained in previous studies ⁴. The names of the CFOs to whom the questionnaire was sent were found on the companies' web sites. In order to make sure that the questionnaire was understandable, we followed Graham and Harvey (2001) and ran a pretest on MBA students in advanced finance courses and also consulted with survey specialists ⁵. Each manager received a personal letter attached to our survey, describing the importance of his/her response. We also offered to send the results of the study to whoever was interested. Moreover, in order to increase the response rate, we phoned some of the managers who had expressed concerns, and promised them that the information they provided would be used for academic purposes only, and would be kept completely anonymous. We asked participants to return their questionnaires to us by fax, electronic or snail mail within three months of the date of receipt. The sectors examined were: banking and finance, communication, construction, energy, manufacturing, retail and wholesale, services, technology and transportation. Table 1 summarizes the key characteristics of the firms sampled in the survey.

[Insert Table 1 here]

The table indicates that the total number of firms in each of the five countries sampled ranges between 21 for Japan and 35 for Canada. The number of firms in each sector across the five countries ranges between 9 in the transportation sector and 26 in the manufacturing sector. Also, the mean values across the nine sectors

for three corporate characteristics are as follows. Sales: \$1322 million, percent of foreign sales: 28%, and percent of public ownership: 79%. The results in the table also indicate that the distribution of sectors over countries is reasonable.

In the questionnaire, the managers were asked to evaluate different variables such as methods used for investment appraisal, financial leverage and dividends. The questionnaire was divided by topics. First, we asked about the investment policy, followed by the financing and dividend policies. The questionnaire (which appears in the Appendix) consisted of 12 questions. Differences between two given sectors were evaluated by using a T test, while differences among all sectors (taken together) were evaluated using an F test ⁶. **Pearson correlation test (r) has been also conducted.**

4. Results

The empirical results are presented below in Sections 4.1, 4.2 and 4.3, respectively, for the investment, financing and dividend policies.

4.1 The Investment policy

Table 2 describes the relative importance that managers from different sectors attach to the three main corporate financial policies: investment, finance and dividend. The table demonstrates that for the entire sample, the investment policy is the most important policy, followed by the financing policy and the dividend policy. **This order supports the M&M view, and highlights the imbalance in finance literature in which a lot more attention is paid to capital structure and dividend policy decisions.** The difference between all sectors concerning the relative importance of the three policies is statistically significant only for the financing policy. The order of relative importance is maintained in all sectors except the communication sector, where the financing policy is perceived as the most important policy. In general, managers from the technology sector see these three major policies as less important than managers in other sectors; this is especially true for the dividend policy. The manufacturing and energy sectors accorded the highest degree of importance to the dividend policy. **The dividend-policy relative low importance level found in the technology sector in comparison to the manufacturing and energy sectors is due to the fact that technology firms tend to pay low or no dividend, while manufacturing and energy firms that enjoy relatively stable earnings, tend to pay more dividend. Brav et al. (2005) argue that the**

perception of stability in future earnings affects dividend policy. Investment decisions lead the firm to its desired growth path. The following section discusses sectorial differences with respect to known growth strategies.

[Insert Table 2 here]

4.1.1 Growth strategies

Table 3 presents the relative importance of different growth strategies, by sector.

[Insert Table 3 here]

Table 3 indicates that there are statistically significant differences among all sectors with regard to “penetrating local and foreign markets” and “expanding the company’s product portfolio”. The findings indicate that managers perceive “penetrating the local market” as the most important growth strategy, followed by “expanding the company’s product portfolio”. “Penetrating the local market” was found to be more important in the banking and finance sector and less important to the energy sector, while “expanding the firm’s product portfolio” was more important in the communication and manufacturing sectors and less important in the construction sector. “Penetrating foreign markets” was perceived as more important in the manufacturing sector and less important in the construction and transportation sectors. The findings imply that the relative importance of each growth policy is derived from the sectors’ activities and needs. The banking and finance sector, for example, typically concentrates its main activities locally, while the retail and wholesale and the manufacturing sectors seek broad international business opportunities. New projects are evaluated by investment appraisal techniques in order to determine the extent to which they contribute to the firm’s value and growth. We next describe how frequently well-known investment appraisal techniques are used in the various sectors. **The following section discusses investment appraisal techniques and their relationship to the growth strategies discussed here.**

4.1.2 Investment appraisal techniques

Table 4 demonstrates the frequency of the use of the following investment appraisal techniques: IRR, NPV, PI (Profitability Index), PBP (Pay Back Period), CAPM (Capital Assets Pricing Model), Decision Tree, Sensitivity Analysis and VAR (Value At Risk), in

each sector. It should be noted that these appraisal techniques are not mutually exclusive and can be used simultaneously.

[Insert Table 4 here]

Of the eight investment appraisal techniques examined, there was a statistically significant **difference** with regard to the use of the IRR and the PI. The IRR is the most commonly used technique for the entire sample followed by NPV. **Finance theory maintains that the NPV method is superior to the IRR method, which ought to manifest itself in more frequent use of NPV, but the widespread use of the IRR seems to indicate that it is more convenient for ranking projects. Managers also use the PBP and Sensitivity Analysis more often than the rest of the examined techniques. GH were also surprised by how often PBP is used because it does not take time into account. BJK find in their European survey that PBP is the most commonly used investment appraisal technique, followed by the NPV and the IRR methods. The relatively high use of PBP is likely attributable to its simplicity and convenience. VAR and the PI were used less frequently.**

The most frequent use of the IRR is in the communication sector and the least common use is in the technology sector. The PI is commonly used in the retail and wholesale sector, while it is rarely used in the transportation sector. As shown in the table, the use of the investment appraisal technique is most common in the construction sector and least common in the technology sector. These findings can be explained by the relative ease of predicting cash flows in the construction sector, compared to the technology sector. The CAPM criterion is commonly used in the service and banking and finance sectors and used comparatively infrequently in the energy sector. Surprisingly, the PBP criteria came in third in the entire sample (after the IRR and NPV) even though theory argues that it should not be used at all. The transportation and manufacturing sectors use this criterion more frequently than other sectors do ⁷. **Like GH and BJK, we also find a positive statistically significant relationship between firm size and the use of IRR, NPV and CAPM. This finding stems, in our view, from a broader practical experience and a stronger grasp of financial theory among managers in large firms than small firms.**

With respect to the growth strategies discussed in the previous subsection, a statistically significant positive relationship has been found between the use of the PI technique for investment appraisal and the preference of penetrating into foreign markets and joint ventures ($r=0.221$ and $r=0.202$, respectively; $p<0.03$ for both cases). It might be that given the higher risk involved in foreign investment and joint ventures, a more crude investment appraisal techniques, such as the PI, may be more appropriate than the more conventional NPV and IRR techniques. A positive significant relationship has been also found between sensitivity-analysis technique and merger and acquisitions (M&A) growth strategies ($r=0.257$, $p<0.01$). Given the high complexity that typically characterizes M&A deals, sensitivity analysis can be helpful technique in examining the different possible outcomes of M&A.

4.2 The Financing Policy

In this section, we will examine whether there are sectorial differences in the financial leverage (Debt/Assets) and other related financing preferences. Our results indicate that the financial leverage varies among sectors and this variation is statistically significant. **Our results agrees with those of Harris and Raviv (1991), Schwartz and Aronson (1967) and Long and Malitz (1985) who found similar leverages within a specific industry.** Table 5 indicates that the mean financial leverage for all the companies surveyed was 56% with a standard deviation of 22%.

[Insert Table 5 here]

The lowest financial leverage found is for the technology sector, while the highest is for the banking and finance sector. **These results agree with those of Beattie et al. (2006) and Miao (2005) who found that the financial leverage would be lower for high-tech firms than for utility firms.** We now split our database to two groups: high and low risk industries. **The division has been conducted according to the non-leveraged beta estimated for each of the sectors in the sample. This beta should represent the sector business risk. The mean non-leveraged beta for the high and low risk sectors were 0.64 and 0.33 respectively (the difference between the high and low risk groups of sectors was statistically significant).** The high-risk sub sample includes the communication sector, construction, energy, manufacturing and technology. The low-risk

sub sample includes Banking and finance, retail and wholesale services and transportation. The mean financial leverage of the high-risk sectors is 49% while a low risk sector has a mean financial leverage of 66% **(and the difference is statistically significant)**. These results imply that, as discussed in section 2, high-risk industries adopt low levels leverages and vice versa. These findings accord with those of Miao (2005) who found a negative correlation between the industry's financial risk and business risk across industries.

Sectors can differ not just in terms of their use of financial leverage but also in terms of their preferences for various sources of funding. Table 6 presents the frequency of use of different sources of funding by sector. The table demonstrates that retained earnings, on average, are the most important source of funds, followed by long-term debt. **These results agree with the pecking order theory of capital structure established in the financial literature.** Across all sectors, the least commonly used form of funding is convertible and warrant financing. Statistically significant differences among the sectors are evident in the frequency of use of the following sources of funds: retained earnings, long-term debt and common equity. Retained earnings are used most frequently in the banking and finance sector and least frequently in the service sector. Long-term debt is more common in the transportation and energy sectors than in the technology sector. Common equity financing is used more frequently in the technology and communication sectors and less often in the retail and wholesale, construction and transportation sectors. **These differences are due, in our view, to the risk level of the sector. High tech sectors, for example, are riskier than utilities. Therefore, we would expect the former to depend more on risk sharing finance (common equity) than the latter.**

[Insert Table 6 here]

4.2.1 The relative importance of various factors for the financing policy

Table 7 summarizes the importance of various factors for the financing decision, by sector. Overall, the most influential factor for the financing decision is projected cash flow, followed by financial flexibility and stock market value (These results agree with those of GH (2001) and BJK (2004)). **No statistically significant differences have been found between the technology sector and the utility sector with respect to the**

relative importance of the projected cash flow (as was found also by Beattie et al. (2006)). Bankruptcy costs and taxes are less relevant to the financing decision. These results disagree with Miao (2005) who found that bankruptcy costs affect the financial leverage decision. There are statistically significant differences among sectors with respect to the effect of the corporate tax rate and the credit rating on the financing decision. The corporate tax rate and the firm's credit rating are the most influential factors in the banking and finance sector and least influential in the technology sector. The technology sector's financing decision is mainly influenced by projected cash flow and stock price. **Finance theory dictates that the positive impact of the corporate tax on the value of the firm is due to the tax deductibility of the debt interest payments. The higher financial leverage usually employed in the banking and finance than in the technology sectors (see Table 5) makes the corporate tax and the debt rating, more relevant to valuation of high leverage industries.**

[Insert Table 7 here]

4.3 The Dividend Policy

As mentioned in section 4.1, managers in our survey consider dividend policy the least important of a firm's three major financial policies. Table 8 summarizes the dividend policies of the sectors examined.

[Insert Table 8 here]

The table indicates that substantial differences exist among the sectors. A constant sum per-share is the most common dividend policy in the following sectors: retail and wholesale, services, manufacturing and transport. On the other hand, the construction, energy, communication and technology sectors are characterized by a high percentage of firms that do not pay dividends at all. The banking and finance sector is the only one in which the dividend policy as a percentage of net income is preferred. These results indicate that firms that operate in sectors that are characterized by relatively stable cash flows (such as the services' industry) prefer to pay a constant sum per-share, while

sectors that have uncertain cash flows (such as the technology sector) prefer not to pay any dividends at all. **These results agree with Brav et al. (2005) who, as mentioned above, argue that the perception of stability in future earnings affects dividend policy, as in Lintner (1956).**

In order to investigate the extent to which the dividend policy differs across sectors we ranked the sectors by the percentage of companies in the sector that pay dividends. Using this variable, we divided all of the sectors into two groups-those in which the percentage was significantly high and those in which the percentage was relatively low. As discussed in Section 2, sectors with higher dividend pay out ratios generally have companies with lower levels of risk, larger sizes and a smaller stock price multiplier. Two risk variables were also considered: the debt rating and the stock price multiplier. The findings are summarized in Table 9.

[Insert Table 9 here]

The table demonstrates that in the sectors in which there is a large percentage of firms that pay dividends, the debt rating is better (i.e., debt is less risky), the price multiplier is smaller and the size of the companies is bigger. **The differences between the two groups of sectors are statistically significant at the 5% level with respect to the percentage of dividend-paying firms and size, and at the 10% level with respect to the price multiplier and the debt rating.**

4.3.1 The relative importance of various factors for the dividend policy

We asked the CFOs to what extent various factors influence their dividend decision. The results are summarized in Table 10. Of the six factors included in the questionnaire, managers reported that the most influential factor for the dividend decision is projected cash flow, followed by the stock price. **Kalay and Michaely (2000) as well as others, have also argued that dividend policy influences the firm's stock price. Here we find that the influence on the stock price is highly considered by decision makers when they make dividend policy decisions.**

The firm's stock price is the only factor that varied statistically among the sectors. While in the communication and energy industries the stock price is an important factor in making dividends decisions, it is less important in the manufacturing and technology sectors. In the technology sector the stock price is regarded as an important factor in the financing decision, but less relevant to the dividend decision, probably because few technology companies pay dividends.

[Insert Table 10 here]

4.4 The imitation effect

In addition to industry-specific needs that dictate different financial behavior across industries, companies in each industry imitate the financial behavior of other companies in the sector (the imitation effect). Companies may utilize this imitation effect in order to save resources needed to construct a unique financial policy. The corporate manager's underlying belief is that the financial policy commonly used in the sector suits his/her needs as well. With respect to the dividend policy, for example, though no direct question about the imitation effect was incorporated in the questionnaire, under the "other" category of responses, about 10% of the managers stated explicitly that they imitate the sectorial dividend policy. We estimate that this result actually understates the real magnitude of the imitation effect in corporate financial policy, for at least two reasons: (1) as stated above, no response category in the questionnaire explicitly addressed the imitation effect; and (2) managers might be reluctant to admit that they imitate the sector's financial policy, tending instead to claim that they construct their own financial policy.

5. Summary and Conclusions

In this study, we have researched sectorial differences in three main corporate finance policies: investment, financing and dividends. We used a multinational survey that was distributed among CFOs of five countries: the US, UK, Germany, Canada and Japan. We received 140 fully completed questionnaires, upon which we based our survey sample results. Our finding demonstrates that for the entire sample, the investment policy is the

most important policy, followed by the financing policy and the dividend policy. **This order supports the M&M view and highlights the imbalance in the finance literature in which a lot more attention is paid to capital structure and dividend policy decisions. This stems from the emphasis on capital markets based research that lends itself to studying these topics and not investment appraisal type decisions.**

The difference between all sectors concerning the relative importance of the three policies is statistically significant only for the financing policy. The order of relative importance is maintained in all sectors except the communication sector, where the financing policy is perceived as the most important policy.

We found that the use of well-known investment appraisal techniques is most common in the construction sector and least common in the technology sector. The IRR is the most commonly used technique for the entire sample. The most frequent use of the IRR was found in the communication sector; the IRR was used least frequently in the technology sector. Penetrating the local market was found to be more important to the banking and finance sector and less important to the energy sector, while expanding the firm's product portfolio was more important to the communication and manufacturing sectors and less important to the construction sector.

The lowest financial leverage has been found in the technology sector while the highest was found in the banking and finance sector. Retained earning is the most common source of financing, followed by long-term debt. Moreover, long-term debt financing is relatively common in the transport, energy and services sectors and relatively rare in the technology sector. The technology and communication sectors finance investments by common equity, which is used less frequently in the retail and wholesale, construction and transport sectors.

A constant sum per-share is the most common dividend policy in the following sectors: retail and wholesale, services, and manufacturing and transportation. On the other hand, the construction, energy, communication and technology sectors have the highest percentage of firms that do not pay dividends at all. Banking and finance is the only sector in which the dividend policy- percent of net income is preferred. Sectors that are likely to pay dividends are dominated by large companies with good debt ratings.

A possible explanation for the differences among sectors found in our study, **with respect to the financing and dividend policies** can be attributed to (1) the unique financial needs and operational condition of each sector and (2) the imitation effect. We believe that companies imitate the financial behavior of other companies in their sector. Our survey **suggests** the existence of the imitation effect, though further investigation of this issue **is needed**.

Footnotes

1. **See, for example, Beattie et al. (2006) and Dhanani (2005).** Graham and Harvey (2001) made a distinction between manufacturing and other industries.
2. Fixed dividend per share over time.
3. The methodology section is similar to that in Cohen and Yagil (2008).
4. Graham and Harvey (2001), for example, obtained a 9% response rate on a survey intended for American managers.
5. Some of the students in the class were from different countries.
6. To simplify the writing, the statistical significance of the difference between two different sectors (calculated by the T test) is not stated in the text. However, all differences between any two sectors described in the text are statistically significant, unless explicitly stated otherwise.
7. **It might be worth noting that in addition to the information provided by Table 4, we also examined the relationship between firm size and the frequency it uses investment appraisal techniques.**

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Table 1: The Characteristics of the Companies Surveyed, by Sector

	Number of firms						Sales (M\$)	Foreign % Sales	Public % Ownership
	US	UK	Germany	Canada	Japan	Total			
Banking and Finance	2	2	3	4	2	13	2,140	25	76
Communication	1	4	2	2	3	12	850	30	81
Construction	1	3	2	2	1	9	740	25	81
Energy	3	3	4	7	2	19	800	20	72
Manufacturing	6	5	5	6	4	26	3,500	35	68
Retail and Wholesale	3	2	4	4	2	15	2,400	40	62
Services	2	4	4	3	3	16	650	25	90
Technology	6	4	3	5	3	21	70	25	91
Transportation	3	1	2	2	1	9	750	30	93
Total number of firms	27	28	29	35	21	140			
Mean							1,322	28	79

Notes: 1. Figures about total sales, percentage of foreign sales and percentage of public ownership are based on Question 11.

2. Sales are annual sales in Million \$.

3. % of Foreign sales represent the percentage of foreign sales out of total sales.

Table 2: The Relative Importance of the Three Major Financial Policies - Investment, Financing and Dividend - by Sector

	Investment	Financing	Dividend	Mean
Banking and Finance	4.54	3.92	2.92	3.79
Communication	4.07	4.14	2.93	3.71
Construction	4.25	3.13	2.43	3.27
Energy	4.21	4.10	3.16	3.82
Manufacturing	4.27	4.06	3.16	3.83
Retail and Wholesale	4.00	3.92	2.42	3.44
Services	4.10	4.00	2.70	3.60
Technology	4.00	3.43	2.05	3.16
Transportation	3.80	3.60	2.80	3.40
Mean	4.13	3.81	2.73	
Significance	0.46	0.00	0.15	

- Notes:** 1. The results are based on the responses to Question 8: How important are the following financial policies to your company? (1=Not important, 5=Very important)
2. “Significance” refers to the significance level of the F test for equality of means.

Table 3: The Relative Importance of Various Growth Strategies, by Sector

	Penetration of Local Markets	Expanding the Product Portfolio	Penetration of Foreign Markets	Strategic Alliances	Mergers and Acquisitions	Joint Ventures
Banking and Finance	4.6	3.9	2.7	3.5	2.6	3.2
Communication	4.3	4.0	3.7	3.6	3.6	3.4
Construction	3.6	2.5	2.6	3.0	2.7	3.7
Energy	2.8	3.4	2.9	3.8	3.6	3.4
Manufacturing	3.8	4.0	4.1	3.4	3.4	3.1
Retail and Wholesale	4.2	3.3	3.9	2.8	3.0	2.7
Services	3.9	3.5	3.2	2.4	3.2	2.6
Technology	3.6	3.8	3.2	3.4	3.3	2.7
Transportation	3.2	3.0	3.0	3.4	3.4	3.0
Mean	3.8	3.5	3.3	3.3	3.2	3.1
Significance	0.00	0.00	0.00	0.16	0.37	0.61

Notes: 1. The table summarizes the answer to Question 2: How important are the following factors for your firm's growth? (1=Not important, 5= very important).

2. "Significance" refers to the significance level of the F test for equality of means.

Table 4: The Frequency of the Use of Investments Appraisal Techniques, by Sector

	IRR	NPV	PBP	Sensitivity Analysis	CAPM	VAR	PI	Decision Tree	Mean
Banking and Finance	3.58	3.62	3.15	3.33	2.67	2.75	1.40	1.55	2.75
Communication	4.67	4.21	3.36	3.71	2.46	2.08	2.67	1.92	3.13
Construction	4.25	3.87	4.25	3.63	1.75	2.13	2.50	2.13	3.06
Energy	4.30	4.20	3.15	3.74	1.44	1.89	1.61	1.67	2.75
Manufacturing	3.78	3.76	3.96	3.51	2.12	2.02	2.39	2.08	2.95
Retail and Wholesale	3.55	3.18	3.83	3.36	2.09	2.36	3.00	1.73	2.88
Services	4.56	4.00	4.00	3.11	2.67	1.78	1.67	1.89	2.96
Technology	3.10	3.86	2.95	3.67	1.74	1.74	1.42	1.95	2.55
Transportation	4.40	3.60	4.00	4.00	2.25	1.25	1.25	2.75	2.93
Mean	4.02	3.81	3.63	3.56	2.13	2.00	1.99	1.96	
Significance	0.03	0.74	0.55	0.87	0.23	0.80	0.05	0.53	

Notes: 1. The results are based on the responses to Question 1: How frequently does your firm use the following techniques for investment appraisal? (1=Never, 5=Always).

VAR = Value at Risk, PBP=(Pay Back Period), PI=(Profitability Index).

2. "Significance" refers to the significance level of the F test for equality of means.

Table 5: The Financial Leverage by Sector (%)

	Mean	Standard Deviation	Min	Max
Banking and Finance	72	18	50	93
Communication	43	23	14	79
Construction	72	28	30	80
Energy	51	22	10	87
Manufacturing	51	21	9	85
Retail and Wholesale	63	19	35	94
Services	62	16	45	85
Technology	26	26	0	83
Transportation	67	23	40	90
Mean	56	22	26	86
Significance	0.00	-	-	-

Notes: 1. Figures based on responses to Question 5: What is your firm's ratio of total liabilities to total assets?

2. "Significance" refers to the significance level of the F test for equality of means.

Table 6: The Frequency of Various Sources of Funds Used to Finance New Investments, by Sector

	Retained Earnings	Long term Debt	Short term Debt	Common Equity	Convertibles	Warrants
Banking and Finance	4.45	2.55	2.91	2.50	1.89	1.11
Communication	3.79	3.31	2.85	3.25	1.69	1.69
Construction	3.88	3.38	3.25	2.00	1.75	1.14
Energy	4.00	4.10	3.30	2.89	1.47	1.47
Manufacturing	4.12	3.43	3.08	2.06	1.54	1.44
Retail and Wholesale	3.50	3.58	2.92	1.83	1.67	1.08
Services	3.11	4.00	4.00	2.56	1.67	1.43
Technology	3.24	2.45	2.05	3.52	1.60	1.57
Transportation	4.20	4.20	2.75	2.00	1.80	1.50
Mean	3.81	3.44	3.01	2.51	1.67	1.38
Significance	0.00	0.00	0.07	0.00	0.96	0.87

- Note:** 1. The findings are based on Question 3: How frequently does your firm use the following sources of funds to finance a new investment? (1=Never, 5=Always)
 2. “Significance” refers to the significance level of the F test for equality of means.

Table 7: The Importance of Various Factors for the Financing Decision, by Sector

	Corporate Tax rate	Personal Tax rate	Bankruptcy Costs	Voting Control	Projected Cash Flow	Credit Rating	Stock Price	Transaction Costs	Financial Flexibility
Banking and Finance	4.25	1.86	1.57	3.67	4.62	3.86	3.29	3.43	4.13
Communication	3.86	1.93	1.86	3.62	4.57	2.93	3.93	2.93	3.50
Construction	2.52	1.83	1.51	2.05	4.06	2.63	3.32	3.34	3.82
Energy	3.50	1.75	2.63	2.90	4.55	3.25	3.67	3.59	3.81
Manufacturing	3.55	1.81	1.97	3.11	4.54	3.29	3.26	3.03	3.70
Retail and Wholesale	3.02	2.14	2.22	2.43	4.52	3.64	3.61	3.42	3.94
Services	3.00	1.13	1.50	3.43	4.88	2.75	3.00	3.00	3.63
Technology	2.22	1.50	1.59	2.65	4.18	2.11	3.95	3.22	3.28
Transportation	4.00	2.00	1.25	2.25	4.60	3.80	3.25	2.80	3.80
Mean	2.99	1.77	1.79	2.90	4.50	3.42	3.48	3.19	3.73
Significance	0.00	0.45	0.10	0.19	0.42	0.03	0.61	0.56	0.46

Notes: 1. The findings are based on Question 4: Indicate the relative importance of the following factors when you make a financing decision. (1=Not Important, 5=Very Important).

.Bankruptcy Costs= potential bankruptcy costs .2

3. "Significance" refers to the significance level of the F test for equality of means

**Table 8: The Frequency of Use of Different Dividend Policies
by Sector (%)**

	Constant sum per-share	Percent of net income	No Dividend	Other
Banking and Finance	23.1	38.5	15.4	23.0
Communication	30.8	23.1	38.5	7.6
Constriction	37.5	12.5	37.5	12.5
Energy	25.0	20.0	50.0	5.0
Manufacturing	42.0	28.0	14.0	16.0
Retail and Wholesale	58.4	16.7	16.7	8.2
Services	40.0	30.0	30.0	0.0
Technology	9.5	14.3	66.7	9.5
Transportation	60.0	20.0	20.0	0.0
Mean	36.25	25.5	32.8	8.1

- Notes:** 1. The results in the table are based on Question 6: Which of the dividend policies best describes your company's dividend policy?
2. Constant sum per-share includes constant sum per-share with minor changes or a special dividend
3. Percent of net income includes percent of net income +growth factor.

Table 9: The Percentage of Dividend-Paying Firms and Related Factors

	Size	M	Rating	of firms that % pay dividends
Banking and Finance Manufacturing, Retail and , Wholesale, Transportation	4.06	18.04	2.85	83.50
Communication, Services, Construction, Energy, Technology	3.16	19.45	3.06	56.50
Mean	3.61	18.75	3.01	70.00
Significance	0.00	0.08	0.09	0.00

Notes: 1. Size is measured by annual sales revenue category (1=less than \$25
6=more than \$5 billion)

2. M=the stock price multiplier (P/E).

.Rating= the firm's least risky debt rating (1=AAA, 6=B) 3

4. "Significance" refers to the significance level of the T test for equality of means.

Table 10: The Importance of Various Factors for the Dividend Policy Decision, by Sector

	Return on Investment	Alternative Return	Stock Price	Dividend Tax Rate	Forecasted cash flows	Cost of New Fund
Banking and Finance	4.00	2.57	2.75	2.17	3.75	3.43
Communication	3.50	3.25	4.25	2.25	3.89	2.63
Construction	3.75	2.25	3.00	1.25	3.60	2.25
Energy	3.20	2.64	4.07	1.54	4.00	2.71
Manufacturing	2.91	2.28	2.69	1.94	3.56	2.42
Retail and Wholesale	3.64	2.64	3.29	1.64	3.64	2.64
Services	3.17	2.50	3.14	1.17	3.67	2.00
Technology	2.67	2.33	2.36	1.36	3.25	3.18
Transportation	1.75	2.50	3.67	1.00	3.25	2.50
Mean	2.76	2.55	3.24	1.59	3.62	2.64
Significance	0.27	0.83	0.01	0.15	0.94	0.58

Notes: 1. The results in this table are based on Question 7: Indicate the importance of the following factors in forming your company's dividend policy (1=Not Important, 5=Very Important).

2. Return on Investment=the rate of return on the company's investments;
Alternative Return=the alternative return (outside the firm) for shareholders;

Stock Price=the impact of the dividend on the company's stock price.

3. "Significance" refers to the significance level of the F test for equality of means.

Appendix Questionnaire

1. How frequently does your firm use the following techniques for investment appraisal?

Never					Always		Never					Always	
1	2	3	4	5		1	2	3	4	5			
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	a) Net Present Value (NPV)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	e) Capital Assets Pricing Model		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	b) Internal Rate of Return (IRR)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	f) Financial Decision Tree		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	c) Profitability Index (PI)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	g) Sensitivity Analysis		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	d) Pay Back Period(PBP)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	h) Value at Risk (VAR)		

2. How important are the following factors for your firm growth? (Not important, Very important)

Not					Very	
1	2	3	4	5		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	a) deepening penetration of local markets	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	b) expanding the company's product portfolio	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	c) penetration of foreign markets	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	d) mergers and acquisitions	<input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	e) joint ventures	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	f) strategic alliances	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	g) other _____	

FINANCING POLICY

3. How frequently does your firm use the following sources of funds to finance a new investment?

Never					Always		Never					Always	
1	2	3	4	5		1	2	3	4	5			
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	a) retained earnings	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	e) short term debt		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	b) external common equity	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	f) convertibles		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	c) internal common equity	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	g) warrants		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	d) long term debt	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	h) other _____		

4. Indicate the relative importance of the following factors when you make a financing decision. (1=Not Important, 5=Very Important)

Not					Very						
1	2	3	4	5	1	2	3	4	5		
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	a) the corporate tax rate	f) the company credit rating
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	b) personal tax rate of your debt holders and shareholders	g) the market value of firm's stocks
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	c) the potential cost of bankruptcy	h) the transaction costs
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	d) voting control	i) financial flexibility
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	e) projected cash flow	j) other _____

5. What is your firm's ratio of total liabilities to total assets? _____

DIVIDEND POLICY

6. Which of the following dividend policies best describes your company's dividend policy? (Check one policy only)

- a) constant sum of money per share
- b) percent of the firm's net income _____%
- c) minor changes in the constant dividend per share
- d) percent of the firm's net income + growth factor
- e) constant dividend per share plus special dividend
- f) other _____

7. Indicate the importance of the following factors in forming dividend policy (1=Not important, 5=Very Important)

Not					Very					
1	2	3	4	5	1	2	3	4	5	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	a) the rate of return on the company's investments
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	b) the alternative return (outside the firm) for shareholders
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	c) the impact of the dividend on the company's stock price
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	d) the dividend tax rate
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	e) the forecasted cash flows
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	f) the cost of raising new funds
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	g) other _____

GENERAL QUESTIONS

**8. How important are the following financial policies to your company?
(1=Not important, 5=Very important)**

Not							Very	
1	2	3	4	5				
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	a) Investment Policy			
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	b) Capital Structure Policy			
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	c) Dividend Policy			

9 Please approximate your firm's average price /earnings ratio over the past 3 years _____

10. What is the credit rating for your firm's least risky debt? (AAA etc..) _____

11. Please choose one item from each category that best describes your company.

<u>Annual Sales Revenue</u>	<u>Industry</u>	<u>% Foreign sales</u>	<u>Ownership</u>
<input type="checkbox"/> a) less than \$25 million	<input type="checkbox"/> a) Retail and Wholesale	<input type="checkbox"/> a) 0%	Public ___%
<input type="checkbox"/> b) \$25-\$100 million	<input type="checkbox"/> b) Construction	<input type="checkbox"/> b) 1-25%	
<input type="checkbox"/> c) \$100-\$500 million	<input type="checkbox"/> c) Manufacturing	<input type="checkbox"/> c) 25-50%	
<input type="checkbox"/> d) \$500 million – \$1billion	<input type="checkbox"/> d) Energy	<input type="checkbox"/> d) >50%	
<input type="checkbox"/> e) \$1 billion- \$5 billion	<input type="checkbox"/> e) Transport		
<input type="checkbox"/> f) more than \$5 billion	<input type="checkbox"/> f) Communication		
	<input type="checkbox"/> g) Bank/Finance/Insurance		
	<input type="checkbox"/> h) Other _____		

12. Your company's headquarters are in what country? _____.

Yes; I am interested in receiving a short summary of the findings of this international corporate finance research. My E-mail is _____.