European Journal of Political Economy 34 (2014) S25–S31

Contents lists available at ScienceDirect

European Journal of Political Economy

journal homepage: www.elsevier.com/locate/ejpe

Bank dividend policy and the global financial crisis: Empirical evidence from Europe

Tobias Basse [a,b,*], Sebastian Reddemann [b,c], Johannes-Jörg Riegler [a], J.-Matthias Graf von der Schulenburg [c]

[a] Norddeutsche Landesbank (NORD/LB), Friedrichswall 10, 30159 Hannover, Germany
[b] Touro College Berlin, Am Rupenhorn 5, 14055 Berlin, Germany
[c] Leibniz Universität Hannover, Königsworther Platz 1, 30167 Hannover, Germany

ARTICLE INFO

Article history:
Received 16 July 2012
Received in revised form 23 August 2013
Accepted 3 September 2013
Available online 13 September 2013

JEL classification:
E3
G1
G3

Keywords:
Dividend policy
Dividend signalling
Regulation
Bank capital base
Cointegration analysis
Financial crisis

ABSTRACT

The global financial crisis has caused controversial discussions about the capital base of the banking industry in Europe. Dividend cuts and omissions have been suggested as one possibility to improve the financial strength of banks by retaining earnings. However, there are fears that investors could interpret a reduction of dividends as a sign for future problems. The dividend signalling and dividend smoothing hypotheses quite clearly are the theoretical basis for these worries. The basic idea of this study is that without empirical evidence supporting the hypothesis dividends did matter in the past, banks should not fear dividend cuts or even dividend omissions. The empirical evidence from the European banking industry reported here does not indicate that dividend signalling and dividend smoothing are relevant economic phenomena.

© 2013 Elsevier B.V. All rights reserved.

1. Introduction

The world economy has suffered from the consequences of the global financial crisis. The banking sector was hit especially hard. Therefore, it is no surprise at all that stock prices of banks all over the world have dropped significantly. While the problems clearly originated in the U.S. housing market many European banks have also been affected by the crisis. These major difficulties of the financial services industry resulted in bailouts and nationalizations. There also is a time dimension to the problem. At first, losses at banks were directly related to the U.S. subprime crisis (mortgage backed securities and collateralized debt obligations). Then the global recession increased the volume of nonperforming loans and caused falling stock prices and a widening of credit spreads. Meanwhile, fiscal problems of some European countries even have caused concerns about sovereign credit risk. At the moment, new (and higher) capital requirements as already codified in Basel II, rating downgrades of debtors and expected future loan losses will increase the demand for capital. Moreover, as a reaction to the crisis there are discussions to further tighten bank capital standards (e.g., Rajan, 2009; Bullard et al., 2009). In sum, the banking sector not only in Europe has been, still is and most certainly will be in need of additional capital.

* Corresponding author at: Norddeutsche Landesbank (NORD/LB), Friedrichswall 10, 30159 Hannover, Germany. Tel.: +49 511 361 9473; fax: +49 511 361 98 9473.
E-mail address: tobias.basse@nordlb.de (T. Basse).

0176-2680/$ – see front matter © 2013 Elsevier B.V. All rights reserved.
http://dx.doi.org/10.1016/j.ejpoleco.2013.09.001

Banks only have limited possibilities to strengthen their capital base. Given that numerous banks already had issued new equity raising capital from external sources there was a shortage of capital for financial institutions in 2009. Private investors simply did not want to increase the exposure to banks in their equity portfolios. In many countries governments stepped into the breach and even nationalised some banks. Due to harsh criticism of the bank rescue plans in the U.S. and other countries banks would at the moment experience major difficulties to obtain additional help from governments. Especially the U.S. media criticized that banks used "taxpayer funds" to pay dividends. Meanwhile, stock prices have at least partly recovered. The Dow Jones Stoxx 600 Banks Price Index, for example, has risen considerably from its lows in March 2009. However, it could still prove to be quite expensive for banks to obtain additional capital by issuing new equity. Banks might also decide to reduce their exposure to risk. This would imply that the banking sector would have to lower the supply of credit (at least in the short run — see Buch and Prieto (2012) on long and short run effects of changes to bank capital on loans). However, in a recession economic policymakers certainly are not interested in reducing the availability of bank credit because there are fears that a negative shock to credit supply could further hurt the economic activity. Walsh and Wilcox (1995), for example, have shown that loan supply shocks did have a negative effect on the U.S. output examining data from the 1960s and 1970s. Moreover, Akhter et al. (2010) recently also have provided empirical evidence indicating that the availability of credit helps to avoid poverty. Therefore, economic policymakers surely do not favour a reduction to bank lending in an economic crisis. In fact, the government bailouts in Europe and other parts of the world have mainly been intended to stabilize the availability of credit.

Banks can also improve their capitalisation by cutting or even omitting dividend payments. However, some observers seem to fear that investors and financial analysts could interpret a reduction of dividend payments as a negative signal indicating future problems. These discussions do have a history. In fact, Mayne (1980) has noted that U.S. banks used dividend cuts to improve their capital base in the banking crisis of the years 1973 to 1976. More recently, Boldin and Leggett (1995) have argued that retained earnings were the primary source of capital for the U.S. banking industry after the savings and loan crisis. However, Bessler and Nohel (1996) have pointed out that bank managers in the U.S. were reluctant to cut dividends in the 1980s despite suffering losses. After the subprime crisis the Federal Reserve, for example, in early 2012 did not want to permit Citigroup to raise its dividend in order improve the ability of the bank to cope with future financial shocks. Interestingly, the financial press had reported that shareholders back then had been pressuring U.S. banks to pay higher dividends.[1]

Given these controversial discussions about dividend cuts we plan to empirically analyse the dividend policy of the European banking industry using a framework that has recently been suggested by Reddemann et al. (2010) More precisely, we are searching for hints indicating that dividend signalling or dividend smoothing are relevant economic phenomena using vector autoregressive models (VAR) (respectively vector error correction models (VECM)). In short, the basic idea of this study is that without empirical evidence supporting the hypothesis that dividends did matter in the past, analysts and other stakeholders should not react on or fear dividend cuts or even dividend omissions by the respective bank.

The paper is organized as follows: Section 2 discusses dividend policy issues from the perspective of corporate finance theory. Section 3 then provides a literature review focussing on empirical tests of the theories of dividend determination introduced in Section 2. The fourth section describes the data sets examined and discusses some methodological issues. In Section 5 the empirical evidence is presented. The final section concludes.

2. Some thoughts about dividend policy issues

In their seminal paper Miller and Modigliani (1961) have argued convincingly that the dividend policy of a firm is irrelevant assuming that the firm's investment policy is given, capital markets are perfect and taxes do not exist. In this environment higher dividends simply result in lower capital gains. Consequently, the dividend policy of a firm does not have any economic relevance when investors do not prefer dividends to capital gains or vice versa. Therefore, it could be argued that the controversial discussions about dividend cuts or omissions of banks are pointless and that banks should reduce the volume of dividend payments to strengthen their capital base without having to fear any negative consequences.

The dividend irrelevancy hypothesis obviously produces major difficulties in trying to explain the existence of dividends. In fact, there is a dividend puzzle because it can be observed that numerous firms in many countries regularly pay dividends. The corporate finance theory has suggested a number of arguments why dividends may not be irrelevant at all. The most popular approaches to explain the existence of dividend payments are based on agency theory. These theoretical concepts rely on the assumption that the management of a firm is not necessarily motivated to act in the best interest of the owners.[2] In fact, it is quite common to argue that dividend payments lead to a reduction of free cash flow and thereby force the management of a firm to obtain capital from external sources more frequently when new investment projects have to be financed. Raising new capital forces a firm to give information to investment bankers, prospective investors and other economic agents. This process of providing information to financial market participants is assumed to reduce agency costs helping the owners to monitor and control the management of the firm. However, obtaining capital from external sources by issuing new equity generates transaction costs. According to this theory the optimal dividend policy of a firm should minimize the sum of the transaction costs and the agency costs.

---

[1] Reports discussing this problem have, for example, been published by the New York Times and Bloomberg News.

[2] It could also be argued that firms may run out of lucrative investment projects and in this case should return financial funds to investors by increasing dividend payments. However, given that central banks not only in the U.S. and UK have lowered the refinancing costs banks at the moment seem to have many profitable investment opportunities.

دریافت فوری ← متن کامل مقاله

ISIArticles
مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات