

The Determinants of Capital Structure Choice: A Survey of European Firms

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ABSTRACT

We survey managers of firms in sixteen European countries to examine the link between theory and practice of capital structure across countries with different legal systems. The evidence shows that financial flexibility and the earnings per share dilution are the most important determinants of the capital structure decisions of the European managers. Managers also value hedging considerations and use window of opportunity in raising capital. The evidence shows modest support for the trade -off theory but weak support for the pecking order theory or agency theory framework. We find that the major determinants of the capital structure decision of the European managers are similar to that of the U.S. There are also significant differences but no apparent consistent pattern across countries based on the English, French, German and Scandinavian legal systems. This suggests that capital structure choice may be the result of a complex interaction of many institutional features and business practices that is not fully captured by differences in the legal systems.

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How firms make their capital structure decisions has been one of the most extensively researched areas in corporate finance. Since the seminal work of Modigliani and Miller (1958) on the irrelevance of capital structure in investment decision, a rich theoretical literature has emerged that models a firm's capital structure choice employing different frameworks. Several theories such as trade-off theory rely on traditional factors such as tax advantage and potential bankruptcy cost of debt while others use the asymmetric information or game theoretical framework in which debt or equity is used as a signaling mechanism or a strategic tool.¹ Many of these theories have also been empirically tested, yet there is little consensus on how firms choose their capital structure.² In a recent paper, Graham and Harvey (GH)(2001) try to fill this gap by providing evidence on the practice of corporate finance theories through a comprehensive survey of managers of the U.S. firms. Our study attempts to do the same in the European context but differs largely in the focus and the scope of our survey. Unlike GH who examine many aspects of corporate finance including capital budgeting, cost of capital, and capital structure, our survey is focused primarily on capital structure. Our sample, on the other hand, spans 16 European countries: Austria, Belgium, Greece, Denmark, Finland, Ireland, Italy, France, Germany, Netherlands, Norway, Portugal, Spain, Switzerland, Sweden and U.K.

Our study contributes to two different strands of literature. First, most of the capital structure theories have been tested in the U.S. context. Some recent studies have explored this issue in the international context but the evidence is unclear. For example, Rajan and Zingales (1995) and Booth, Aivazian, Demirguc-Kunt, and Maksimovic (2001) compare capital structures across different countries but conclude that although some insights from the U.S. context are portable

across countries, much remains to understand the influence of different institutional features on leverage choices. A major problem in such research is that differences in legal and institutional environment as well as in accounting practices make it difficult to compare and interpret financial data across countries.³ Our study complements this literature because a direct comparison of managerial responses using survey methodology is one way of overcoming this difficulty. Despite its limitations, survey approach also allows us to collect qualitative data that may be difficult to obtain otherwise. Further, by comparing responses of European managers in our survey to those of the U.S. managers in GH (2001) study, we also gain some insights into the common and different determinants of capital structure choice between the U.S. and European firms.

Our paper also contributes to another newly emerging strand of literature that emphasizes the role of legal environment in firms' ability to raise external finance across countries. La Porta, Lopez-de-Silanes, Shleifer, and Vishney (LLSV) (1997, 1998) compare external finance across 49 countries based on English, French, German, or Scandinavian legal systems and find that the countries with better legal protection have more external financing available in both the debt and equity markets. In this study, we examine whether the legal system framework is also useful in capturing the differences in capital structure choice of firms by comparing managerial responses across the English, French, German, or Scandinavian law countries in our sample.

Our survey shows some interesting findings about theory and practice of capital structure choice in European countries. Financial flexibility appears to be the major determinant of the debt policy while earnings per share dilution is the most important concern of the European managers in issuing equity. Hedging consideration is the primary factor influencing the selection of the maturity of debt or when raising capital abroad. We also find that while the major determinants of the capital structure choice are very similar between the European and US managers, the relative importance of these factors differs significantly across different legal system countries. Further, these differences

cannot be explained only by the quality of legal systems, suggesting that capital structure choice may be the result of a complex interaction among many institutional features that may differ across countries.

The rest of the paper is organized as follows. The next section discusses the research design and methodology and discusses the characteristics of the sample firms. The empirical analysis is presented in the next two sections and summary and conclusions in the last section.

1. Methodology

A. Survey Questionnaire

Our survey focuses primarily on the determinants of the capital structure policy of firms but also includes some questions on topics that are closely related to the capital structure. For example, we ask the managers about their approximate cost of equity, how they estimate their cost of equity (with CAPM or other methods), and whether the impact on the weighted average cost of capital is a consideration in their capital structure choice.

The first draft of the survey was developed after a careful review of the capital structure literature pertaining to the U.S. and European countries. For ease of comparability, we tried to keep the format and design of our survey similar to that of Graham and Harvey (2001) but modified or added several questions that are likely to be relevant in the European context. For example, literature suggests that there are strong differences in corporate objectives between Anglo-American and the Continental European financial systems since the former system focuses on maximizing shareholder wealth while the later emphasizes the welfare of all stakeholders including employees, creditors and even the government.⁴ To examine this difference, we ask the CFOs about the extent to which different stakeholders influence their firm's financial decisions. Further, we also ask the firms

whether they have voting or non-voting shares, and the percentage of their free float shares. Finally, a large number of European firms are also listed on foreign exchanges, we ask the firms information about their foreign exchange of listing, foreign sales, and capital raising activities in foreign markets.⁵

The first draft of the survey questionnaire was tested by academics and financial executives in summer 2001 and it was revised after incorporating their suggestions. Our final survey questionnaire is structured around nine topics. We limited the length of the survey to two pages to increase the response rate; tests showed that it took approximately 15 minutes to complete.

B. Sample

Our initial sample for mailing the survey consists of a total of 737 firms from sixteen European countries. The choice of our initial sample was based on selecting firms that are representative of the European firms, are widely traded, are comparable across countries, and have publicly available information. These criteria are important for minimizing firm-specific differences across countries to facilitate cross-country comparisons. The list of non-French firms was obtained from the French Financial Journal *La Tribune*. Two types of firms were reported in this journal: one consists of large firms that are also normally part of the national stock indexes of their country and the other includes small or technology firms that belong to new markets such as European Nasdaq. A total of 621 non-French firms were included from this list. Another 116 French firms were added that are part of the SBF 120 index. From this sample, 17 firms were deleted because of non-availability of addresses, and another 13 firms were deleted because they declined to participate in the survey, leaving a final sample of 707 firms.

Table I presents the size of our initial sample firms measured by market capitalization and total sales in the year 2001. The average market capitalization of these firms is 9,009.5 million euros

but it varies substantially across countries. The Swiss firms in our sample are the largest in terms of market capitalization (19,476 million euro) followed closely by the U.K. firms (15,100 million euro). The Norwegian firms on the other hand, are the smallest with an average market capitalization (970 million euro) of about one tenth of the sample average. These cross-sectional differences are much less pronounced when sales levels are used for comparisons. The average sales level for our sample firms is 8,025 million euro and it varies from a high of 12,822 million euro (Germany) to a low of 1,639 million euro (Denmark).⁶ Overall, our sample represents a broad cross-section of firms from different European countries.

The survey was mailed to the Chief Financial Officers (CFO) of these firms whose names and addresses were obtained from the Bloomberg database.⁷ The survey was anonymous as this was an important criteria to obtain honest responses. Three mailings were undertaken for the survey. The first mailing was done in September 2001, the second in November 2001 and the third in January 2002. In each mailing a letter was included that was addressed to the CFO or CEO explaining the objective of the study and promising to send a copy of the findings to those who wished to receive it. A total of 87 responses were received by mail or by fax, which represents a response rate of 12 percent and is slightly higher than that in Graham and Harvey (2001).⁸

Table II presents the sample firms and compares the percentage of responses by country and by the legal origin of the country. It shows that all legal systems are well represented. The largest number of sample firms (about 45 percent) belong to the French law countries followed by English law (21 percent), German law (19 percent) and the Scandinavian law (15 percent) countries. The largest proportions of respondents are from France, Germany, and U.K. which is not surprising since these countries also represent about half of the initial sample firms. Across countries, the response rates vary substantially but except in one case, the proportions of respondents are not statistically different from that of the sample firms from that country using the Fisher's Exact test. The

multivariate tests across countries and legal systems also support that the respondent firms are representative of our initial sample of the European firms to whom the survey was mailed.

C. Summary Statistics of Respondent Firms

Figure 1 presents the characteristics of the respondent firms. A large proportion of our respondents (over 80 percent) have sales of over \$1 billion euros. The distribution of respondents is, however, more evenly distributed when size is proxied by market value of equity. About 62 percent of respondent firms have market capitalization of less than 1000 million euros or between 1000 million to 5000 million euros.

The respondent firms represent a wide variety of industries with a larger concentration in manufacturing, mining, energy and transportation sectors (about 37 percent), high technology (18 percent), and financial sectors (18 percent). Both growth and non-growth firms are well represented. High growth firms, defined as firms with price to earnings (P/E) ratio greater than 14, comprise about 65 percent of the sample. About 66 percent of the firms are also widely held public firms and about 36 percent have multiple classes of shares. Over 92 percent of the firms are non-utility firms and an overwhelming majority of them (95 percent) pay regular dividends.

About three fourth of firms have a target debt to equity ratio, and about half of these firms maintain a target debt to equity ratio of one. Further, many respondents have a large percentage (over 50 percent) of their total debt in short- term. Over 77 percent of respondents have issued equity, and about 50 percent of them have issued convertible debt during the last ten years. About 80 percent of respondents report that they calculate their cost of equity, and over 77 percent of them employ the Capital Asset Pricing Model (CAPM) to calculate this cost. The estimated cost of equity reported by respondents ranges between 9 percent to 15 percent; only few firms report cost of

capital greater than 15 percent. A vast majority of respondents also report that the financial policy of their firm is influenced largely by the stockholders and much less by other stakeholders.

A majority of the respondent firms are also internationally oriented; about 58 percent have foreign sales greater than 50 percent of total sales, and about the same percentage have issued debt or equity in foreign markets in the last ten years. Over 44 percent of the respondents are also listed on foreign exchanges and about 35 percent of those are listed on both European and US stock exchanges. Overall, a majority of our respondents are large multinational firms that have raised capital in both domestic and foreign markets.

We also collect information on the characteristics of the Chief Financial Executives (CEOs) of the respondent firms. About 58 percent of CEOs are between 50-59 age category, only 19 percent of them are older than 59. Their average tenure is evenly spread in various categories with about 39 percent having tenure of less than 4 years, 28 percent between 4 to 9 years, and 33 percent greater than 9 years. The CEOs of our sample firms are also highly educated; about 68 percent have a Masters degree (40 percent have an MBA), and about 19 percent have a Ph.D. degree. A vast majority of the CEOs and other top managers (about 87 percent) own less than 5 percent of their firm's stock; only about 4 percent own more than 20 percent of their firm's stock.

The correlations among the demographic variables of our survey respondents are largely as predicted in the literature. These correlations are presented in Table XV and discussed in detail in section 5 that also examines the robustness of our results to these variables.

2. Results

A. Theory and Practice of Capital Structure

We asked managers about their opinion on various factors that are likely to influence capital structure policies of firms. Three sets of factors are selected based on a review of literature. The first

set of factors is based on the implications of different capital structure theories such as the trade-off theory, the pecking order theory, and the agency cost theory. The second set relates to the managers' timing of debt or equity issues since literature suggests that managers are concerned about financial flexibility and use "windows of opportunities" to issue debt or common stock.⁹ Finally, the last set of factors is based not on any theoretical considerations but on commonly held beliefs among managers about the impact of capital structure changes on financial statements such as the potential impact of equity issue on earnings. We also asked questions on the determinants of convertible debt and foreign debt and equity. The managers were requested to rank the importance of each factor on a scale of 0 to 4 (with 0 as not important and 4 as very important). In this section, we also examine differences in managerial responses on five firm characteristics that are expected to be highly correlated with leverage: size, industry, P/E ratios, foreign listing status, and the level of foreign sales. In section 5, we extend this analysis to cover other demographical variables for which we collect data in our survey. The summary of responses and their implications are discussed below separately under each policy.

B. Debt Policy

We asked three questions relating to the debt policy. The first question asked the managers how they choose the appropriate amount of debt for their firm? Figure 2 and Table III present the summary of responses. Financial flexibility is ranked as the most important determinant of debt (mean rank=3.39). About 91 percent of the managers rate financial flexibility as either important (rating=3) or very important (rating=4). Credit rating is considered important or very important by 73 percent of managers (mean rating 2.78). Other important factors include the interest tax savings (mean rank 2.59), and volatility of earnings (mean rank 2.33). The concerns of customer/suppliers about firm's financial stability and transaction costs of debt are considered marginally important (mean rank

about 2) but potential costs of bankruptcy or debt levels of industry peers are rated as less important (mean rank <1.9). Factors that relate debt to agency costs or tactical reasons such as to motivate managers to work hard, or to reduce attractiveness of firms as a target are all rated as unimportant (mean rank < 1).

In another related question, we ask managers about other factors that influence their debt policy (Table IV). About 70 percent of respondents rank the lowering of weighted average cost of capital as either important or very important (mean rating of 2.80). This view is consistent with the importance of the tax advantage of debt that received a mean rating of 2.59 in the question relating to the amount of debt (Table III).

The factors relating to the timing of the debt or equity issue are also viewed as modestly important. The level of interest rate and the valuation level of equity in the stock market both received a mean rank of about 2. This evidence supports the notion that managers use windows of opportunity to raise capital. Although transaction costs of debt are considered important, few managers delay the issuance of debt because of the transaction costs. There is also little support for the factors relating to the signaling theory or the pecking order theory. For example, factors such as “issuing debt gives a better impression than issuing debt” or that “we issue debt when recent profits are not sufficient to support our activities” are not considered important by managers.

Another question asked managers’ opinions on the factors driving the choice between short-term and long-term debt (Figure 3 and Table V). About 77 percent of the respondents consider the matching principle, matching the maturity of debt with the maturity of assets, as either important or very important factor (mean rank=3.10). About 70 percent of the managers agree with the view that issuing long-term debt minimizes the risk of refinancing in bad times and it is an important consideration in issuing debt (mean rank=2.83). This view is consistent with the importance of financial flexibility in the first question related to debt.¹⁰ Again, there is some support that managers

select timing of the debt issue since many managers issue short-term debt when they are waiting for the long term interest rates to decline (mean=1.85). There is little evidence that debt is used to reduce agency costs or for tactical reasons. For example, reasons such as issuing short-term debt to capture higher returns for shareholders or to reduce the chance that firm will undertake risky projects are not supported.

As discussed above, there are some differences among firms on the relative importance of different factors based on size, and the percentage of foreign sales (Tables III-V). For example, larger firms consider credit rating as significantly more important than their smaller counterparts and are influenced more by debt levels of their industry peers. They are less concerned about potential bankruptcy costs, and about the volatility of their earnings and cash-flows. Firms with larger percentage of exports, on the other hand, place higher value on financial flexibility and tax advantage of debt than their domestic oriented counterparts do. Surprisingly, there are little differences based on the foreign listing status of firms which suggests that foreign listing of European firms may be driven primarily by considerations other than capital raising.¹¹ The differences based on industry and P/E ratios are also much less pronounced.

C. Common Stock policy

A large number of respondents (over 77 percent) have issued equity in the last ten years and they identify several factors as important determinants of issuing common stock. (Table VI and Figure 4). Earning per share dilution is considered as important or very important factor in issuing equity by about 66 percent of those managers who had undertaken an equity issue (mean rank 2.72). This evidence supports the literature that there is common belief among managers that issuing additional shares has a negative impact on earnings per share. Surprisingly, larger firms are more concerned with the dilution of earnings than are their smaller counterparts. There is also strong evidence that

managers select timing of the equity issue based on their firm's stock price. About 59 percent of the respondents report that issuing stock after a rise in stock price is an important or very important factor (mean rank 2.61). Another related question about the significance of the amount of stock overvaluation or undervaluation in issuing equity also received a similar ranking (mean rank 2.44). This evidence can also be interpreted as consistent with the importance of earning per share dilution since issuing stock after a rise in stock prices is likely to reduce the risk of earning per share dilution (the dilution being an inverse function of the PE ratio).¹² The dilution of certain shareholders' holdings and the ability to issue common stock for paying a target or for using pooling of interest method are, however, rated only marginally important. Overall, this evidence suggests that the managers' decisions are strongly influenced by the impact of equity issue on financial statements of a firm.

Managers consider that maintaining a target debt to equity ratio is an important factor; about 59 percent of managers report that this factor is important or very important (mean rank 2.67). Other reasons that are modestly important include shares for employee stock option plans (mean rank 2.07), and insufficient funds to finance firm's activities (rank=1.94). Inability to obtain funds from other sources, or issuing stock to give a better impression of the firm are considered unimportant, providing less support for the pecking order or signaling theory frameworks. Very few managers, however, believe that common stock is the least risky source of financing.

There are significant differences in the responses between the high growth (defined as P/E >14) and low growth firm (defined as P/E <14) on many dimensions. Compared to the low growth firms, more high growth firms view equity as a less risky and cheapest source of funds and a signal of better impression of the firm, pay more attention to stock price level when issuing equity, use equity issue for employee stock option plan, and are concerned about dilution of equity of certain shareholders and capital gains tax rates faced by their investors (Table VI). Less pronounced

differences are observable in responses based on size, industry or international orientation of the firms.

D. Convertible Debt

Managers highly value convertible debt as an inexpensive way to issue ‘delayed’ common stock and for the ‘ability to call’ or the flexibility to force conversion of convertible debt when they want to (Table VII and Figure 5). These two factors are considered important or very important by about 55 percent of respondents (mean rank about 2.44). Again, consistent with their views on equity issue, managers (especially those of small firms) view the option to issue convertible debt when equity is undervalued (mean rank 2.40), and avoiding short-term equity dilution as important advantages of issuing convertible debt (mean rank 2.16). Other factors such as convertible debt is less expensive than debt or that it is attractive for investors who are unsure about the riskiness of the firm are considered only modestly important with a mean ranking of 1.86 and 1.68 respectively. Factors relating to agency theory such as to protect bondholders against the actions of stockholders or managers are considered relatively unimportant.

There are significant differences on the importance of factors between firms based on size. Larger firms place higher value on the use of convertibles to issue delayed common stock and view convertible as less expensive than debt compared to their smaller counterparts. Less pronounced differences are observed based on growth, industry and foreign sales.

E. Foreign Debt or Equity

A large percentage of our respondent firms have issued debt or equity in foreign markets. Hedging issues are cited as the most important factors by managers who raised capital abroad. (Table VIII and Figure 6). Providing a natural hedge and matching the sources and uses of funds are cited as

important or very important by about 67 percent of managers (mean rank for both about 2.70). These views are similar to and consistent with those in the selection of debt maturity. Favorable tax treatment and better market conditions relative to Europe are also ranked modestly important with a mean ranking of about 2. Surprisingly, while the level of interest rate is considered important by managers when issuing debt in domestic market, it is relatively unimportant (mean rank 1.48) when issuing debt abroad. There are significant differences on the advantage of favorable tax treatment relative to Europe based on size and international orientation of firms; this factor is considered more important by managers of small firms and those not listed on foreign exchanges. Overall, hedging consideration appears to be the driving force in raising capital abroad and there are only minor differences in responses based on firm characteristics.

3. Managerial Responses Across Different Legal System Countries

A large number of previous studies have compared capital structures across countries and find significant differences even among the developed countries. Most of these studies explain these differences using the bank-oriented versus market-oriented frameworks. For example, Rutherford (1988) shows that aggregate debt levels are higher for firms in bank-oriented countries such as Japan, France, and Germany than in the market-oriented countries such as U.S. and U.K.¹³ In a recent study, Rajan and Zingales (1995), examine the influence of different institutional features on capital structure in a comparative study of G-7 countries: United States, Germany, Canada, Italy, France, Japan, and the United Kingdom. They find that leverage and its correlations with variables such as firm size and profitability appear fairly similar across U.S. and other countries but indepth analysis shows that the theoretical underpinnings of the observed correlations are different. They argue that the size or power of banking sector is one but perhaps not the most important institutional

difference in their sample and that the capital structure choice is a consequence of the influence of different institutional structures such as tax codes and bankruptcy laws which need more research.

In recent studies, La Porta et al. (1997,1998) argue that law and quality of its enforcement are important determinants of the ownership structure and the ability of the firms to raise external finance through either debt or equity. They divide countries into two broad categories based on their legal origin: common law and civil law countries where the later is further divided into three categories, French, German, and Scandinavian legal systems and argue that common law countries provide the strongest protection and the French law the weakest protection to creditors and shareholders. They study the impact of these systems in a sample of 49 countries around the world and find that the legal environment and the quality of enforcement is strongly related to the size of the capital markets, the debt and equity policies, and the ownership structure of firms. In this section, we extend this analysis to examine whether the determinants of the capital structure choice also vary systematically across different legal systems by comparing managerial responses in our survey across English, French, German and Scandinavian law countries and with those of the U.S. managers reported in the GH (2001) study. Our main focus is to examine whether legal system typology provides us a rich framework to examine cross-country differences. In such case, we should expect systematic differences in responses across legal system countries. For example, the determinants of capital structure should be similar between U.S. and English law countries and between German and Scandinavian law countries. Any large unsystematic patterns across the legal systems would suggest that institutional features such as tax code, bankruptcy laws or security market governance structure not accounted for by the legal systems may also play a major role in capital structure choice.

This comparative analysis is presented in Tables IX-XIV and Figures 7-11. Columns one and two in each of these tables present the percentage of respondents who consider a factor as important

or very important and the mean rank respectively for all European sample. Columns three and four report the mean rank for each factor for the US firms and the Fortune 500 firms from GH (2001). The next four columns (columns five to eight) in each table present the mean rank for the English, French, German, and Scandinavian Law countries respectively, and the last six columns report the p-values for the t-test of differences in mean ranks for each factor among different legal system countries. The main findings in these tables are discussed below.

A. Debt Policy

The comparison of responses on factors relating to the decision about the amount of debt undertaken are presented in Table IX and Figure 7. The following observations from this comparison are noteworthy. First, the relative rankings of the major determinants of the debt policy are largely similar although their mean rankings are different between the European and the US managers. For example, financial flexibility is ranked important or very important by about 91 percent of the European managers (mean rank=3.39) compared to less than 60 percent of the U.S. managers (mean rank=2.59; see GH, 2001 Table 6, page 213).¹⁴ Similarly, credit rating is considered important or very important by 73 percent of the European managers compared to about 57 percent of the US managers (see GH, 2001, Table 6, page 213). Second, in contrast to the similarities between the European and US managerial responses, there are large differences across different legal systems on many dimensions. More importantly, there appears to be no consistent pattern of rankings across different legal systems. For example, the German and Scandinavian system respondents assign a much higher ranking to the credit rating compared to that of the English or French Law respondents. The tax advantage of interest deductibility, on the other hand, is ranked much higher in both English and French law countries (2.92, and 2.87 respectively) relative to that in the German and Scandinavian law countries (2.33 and 1.93 respectively), and these differences are statistically

significant at less than 0.05 level in all cases. Interestingly, the mean ranking of financial flexibility in English law countries is significantly lower (3.0) than that in Continental European countries (about 3.48) (Table IX, Figure 7). Further, customers / supplier's concern about the level of debt is not important for managers in the English law countries but is modestly important in the non-English law countries. Only a few factors such as debt levels of peers or the volatility of earnings receive similar rankings across all legal system countries.

The European and U.S. managers also have similar views on the major determinants of choice between short- term and long-term debt but the European managers assign a higher mean rank relative to their US counterparts in every case (Table X, Figure 8). Again, there are large variations in rankings across different legal systems. For example, “matching maturity of debt with the life of assets” is ranked much higher in French Law countries (mean rank 3.43) compared to that in the German, Scandinavian, and English law countries and these differences are statistically significant in most cases

Responses to other factors affecting debt policy also show similar patterns of differences across legal systems (Table XI). The use of debt to minimize the weighted average cost of capital is ranked from a low of 2.33 in English Law countries to a high of 3.0 in French Law countries. Issuing debt when the interest rates are low has a similar ranking among the French and Scandinavian Law countries. There are some differences across European and the U.S. managerial responses as well. The use of debt when equity is undervalued is ranked higher by the European managers compared to that of their U.S. counterparts. Similarly, issuing debt when internal funds are not available is considered important or very important by about 47 percent of the US managers (see GH, 2001, Table 9, page 220) but by less than half of that percentage in the European countries. Surprisingly, the English Law countries have the lowest mean rank among all European countries for this factor.

B. Common Stock Policy

The cross-country comparisons relating to determinants of common stock issue (Table XII and Figure 9) show that the responses of the European and the US managers are very similar on most dimensions. Earning per share dilution is viewed as the most important factor by both the European and US managers with very similar ranking (2.72 and 2.84 respectively). The factors relating to the stock performance and the amount of stock undervaluation or overvaluation are also considered important in timing of stock issue by both European and US managers, although their rankings differ slightly between the two groups.

Across the legal systems, however, the differences are even more pronounced than observed in the case of debt policy. Three observations are noteworthy. First, the rankings of Scandinavian law country respondents differ significantly from those of their other European counterparts on almost all factors. For example, earnings per share dilution ranked the highest (about 3) in all non-Scandinavian countries is considered unimportant (mean rank 1.56) in the Scandinavian law countries, and the differences in means are significant at less than 0.05 level in all cases. Factors relating to stock price or stock valuation also receive the lowest ranking in the Scandinavian law countries. As Figure 9 and Table XII show a similar pattern emerges for most other factors. Second, managerial responses in the French and German law countries are very similar on most factors including earnings per share dilution, and target debt to equity ratio. Except in one case, none of the p-values for differences between the French and German managers are statistically significant at any reasonable significance level. Third, the views of managers from the English law countries differ from those of their European and U.S. counterparts on many dimensions. Some factors such as earnings per share dilution are ranked higher (mean rank 3.2) by English law countries compared to their US counterparts (mean rank 2.84) while others such as maintaining a target debt to equity ratio

are ranked much lower by the English law managers (mean rank 1.4) compared to that by the U.S. managers. Similar differences are observable when the responses from the English law countries and the Continental Europe countries are compared.

These observed differences cannot be explained by the quality of law or of legal protection considerations only. The similarity of responses between the French and German law countries and the differences between the Scandinavian or English law countries and their other European counterparts suggest that other institutional factors in addition to the legal environment may also play an important role in determining the capital structures across countries.

C. Convertible Debt

The pattern for the determinants of the convertible debt issue (Table XIII, Figure 10) is largely similar to that observed for the common stock issue. Both European and U.S. managers identify the same factors as important and assign similar rankings to most factors but the differences across European countries are substantial. In particular, French and German law countries' managers assign very similar rankings to most factors but these rankings differ significantly from those of the Scandinavian and English law country managers. For example, the ability to "call" or the flexibility to force conversion of convertible debt is ranked the lowest in English law countries (mean rank 1.75) and the highest in the Scandinavian law countries (mean rank 3.0) while the reverse is true for the short term equity dilution factor. The responses of French and German law countries, on the other hand, are very similar on both of these factors. The difference in rankings between the managers of the Scandinavian law countries and those of the French or German law countries are also statistically significant in numerous cases.

D. Foreign Debt or Equity Policy

A similar pattern is observed in the managerial responses on the foreign debt or equity policy (Table XIV, Figure 11). Both European and U.S. managers identify similar factors as important determinants of the foreign issues and assign similar rankings to these factors. There are substantial differences in responses across European countries, especially between those of the English and French law countries. For example, the top two factors, providing a ‘natural hedge’ and keeping the “source of funds” close to its “use”, are ranked the highest by the managers in the French law countries (mean rank about 3.27) but the lowest by those in the English law countries (mean rank 1.63); the difference is significant at less than 0.05 level in both cases. Surprisingly, none of the specified factors except one, the favorable tax treatment, are ranked important by the Scandinavian law managers (mean rank equals 2). The relative rankings of many factors also differ between the French and German law countries, although these are not statistically significant in most cases.

In summary, there appears to be agreement among European and U.S. managers on major determinants of capital structure, although the rankings of these factors are different. A comparison with the Fortune 500 firms as a benchmark also leads to similar conclusions on most factors, suggesting that the differences in size or investor recognition of the firms is not a likely source of differences between the US and European responses. However, there are significant differences across different legal systems on many dimensions. More importantly, no consistent pattern emerges as would be suggested under the legal system framework. This evidence suggests that the capital structure choice may be a result of complex interaction of many institutional structures including disclosure rules, accounting systems or banking systems that are not fully captured by the legal system distinction.

4. Robustness Tests

In the previous section, we document that managerial responses differ across legal systems on many dimensions. In this section, we examine whether these results could be driven by differences in characteristics of respondent firms or by potential biases and measurement problems that are normally associated with the survey data and methodology. The main objective of these tests is to gauge the confidence level in our findings, to caution the reader wherever necessary in drawing inferences, and to look for some possible clues that may be helpful in furthering research in this area.

A. Firm Characteristics and Capital Structure Choice

In section 3, we examined the sensitivity of responses to five firm characteristics that are likely to be highly correlated with capital structure choice: firm size, P/E ratio, industry, foreign revenue, and foreign listing. In this section, we investigate the sensitivity of our results to a much larger set of variables including the above mentioned five variables. .

The correlations among these variables are presented in Table XV. For ease of exposition, we divide these variables into two broad categories. The first set of variables (Panel A) is similar to that in GH (Table 1, page 195) and is useful for comparisons across European and U.S. responses. The second set of variables (Panel B) is likely to be more relevant in the European context. For example, the first five variables in Panel B proxy the influence of different stakeholders on financing decisions of a firm and these may partly capture the distinction between “bank-oriented” versus “market-oriented” economies that has been used in the previous literature to study cross-country differences in capital structures. Other variables include the types of shares, the percentage of floating shares, and the estimated cost of equity among respondent firms.

Two main observations follow from Table XV. First, the correlations among variables in both Panels A and B are largely as predicted in the literature. For example, high P/E ratio firms are likely to have lower D/E ratio, higher managerial stock ownership, higher percentage of floating shares, and lower estimated cost of equity. Second, the strength of correlations among these variables is, on average, much lower than that in the GH study. Of the 91 possible correlations among Panel A variables, only 14 are statistically significant in our study (with only one at less than 1 percent level). In contrast, 51 of these correlations are statistically significant (32 at less than 1 percent level) in the GH study. A similar pattern of low correlations is also observed among Panel B variables. The low correlations in our sample could partly be driven by strong differences between European and U.S. respondents on certain characteristics. For example, a much higher proportion of our respondent firms are dividend paying and in non-regulated industries compared to that in the GH study. Overall, this analysis suggests that our results are likely to be less sensitive to demographic correlations than that in the GH study.¹⁵

We next examine whether these characteristics differ among respondents across legal systems. As shown in Table XVI, most of the variables in Panel A including size, P/E ratios, or industry are very similar across different legal system respondents, suggesting that the differences across legal systems do not appear to be driven by firm-specific characteristics. There are, however, some notable differences on some dimensions. The English legal system respondents are the most internationally oriented with the highest percentage of reported foreign revenue, followed closely by the Scandinavian law and German law respondents. The English law countries also have the highest percentage of firms listed on foreign exchanges while the German law countries have the lowest. The target debt to equity ratio is, however, the lowest (0.55) among the English law respondents and the highest among the French law respondents (0.89) and the differences are significant at less than 0.05 level. Surprisingly, the debt to equity ratio (measured by the long-term debt over the market

value of equity) is the lowest among the Scandinavian law countries followed closely by the English law countries. The CEO characteristics are similar across most legal systems except that the Scandinavian CEOs are younger and have shorter tenure than their other European counterparts. These differences suggest that managerial responses may be influenced by some other institutional factors in addition to the legal systems.

We next examine Panel B variables to find some clues about underlying forces that may induce these differences. We observe that managerial responses from the Scandinavian law countries differ significantly from that of other European countries on several dimensions.¹⁶ The Scandinavian respondents have the largest proportion of multiple classes of shares (64%), lowest debt to equity ratio (0.18), and highest percentage of dividend paying firms (100%) relative to their European counterparts. However, some of these differences are puzzling as the Scandinavian respondents also share many common features with their European counterparts. For example, while the influence of shareholders on financing decisions is the lowest among Scandinavian country respondents, that of other stakeholders including creditors and employees is very similar to that of other respondents. Also, these differences can not be attributed to differences in the ownership structure (widely held firms versus closely held) or to the percentage of free floating shares both of which are higher in Scandinavian respondents relative to that in French or German law respondents. Thus, while these differences suggest that there are some underlying institutional factors that strongly influence the capital structure in Scandinavian countries, what these factors are is not easy to discern from our data. For example, the Scandinavian respondents report the highest estimated cost of equity (14 percent) relative to their other European counterparts (about 10 percent). This implies that the Scandinavian country firms should rely more on debt than on equity financing. Yet, the target debt to equity ratio as well as the percentage of Scandinavian respondents that have issued equity in the last ten years as well as their target debt to equity ratio is similar to that of other

respondents. Interestingly, the percentage of Scandinavian respondents who use CAPM for estimating the cost of equity is about half (40%) of that in other countries. Whether the use of CAPM has any relation with the reported estimated cost of equity or is a spurious correlation is difficult to examine in our data.

Since literature suggests that industry is closely related to capital structure and industrial structures differ significantly across European countries, it is plausible that the observed differences in the responses across legal systems could be driven by the differences in industries.¹⁷ To examine this possibility, we analyze the correlation between industry and legal systems across eight industrial categories used in our survey (Table XVII). This table shows that almost all industrial categories are represented in all legal systems but there are differences in proportions of industrial representation across legal systems. In particular, Scandinavian countries have a higher than average percentage of manufacturing and high technology respondent firms and none from the mining and construction sectors. Similar differences are observed across other legal systems. To test the significance of these differences, we conduct contingency table analysis that tests the independence between legal system and industry category variables. The value of the Chi-square test statistic is 18.38 which is not significant at any reasonable level (p-value 0.63). This analysis suggests that the differences in our results across legal systems do not appear to stem from differences in industrial structures.

In summary, the pronounced differences among Scandinavian respondents relative to their other European counterparts on some dimensions support our main conclusion that legal system typology may not fully capture the complex interaction among institutional factors that influence the capital structure choice. What these factors are is beyond the scope of this paper and is left for future research to explore.

B. Survey Data and Methodology

Two major problems in survey data and methodology are: (i) response validity i.e. whether the respondents have truthfully answered the questions asked in the survey and (ii) nonresponse bias i.e. whether the respondents are representative of the population studied. We examine these two biases in our data below.

B.1. Response Validity

To what extent the responses reflect the reality in the field is impossible to test directly. Our modest aim is to test the validity of our general conclusions rather than that of responses. One way to test this is to get feedback on our findings from practitioners who are knowledgeable about capital structure choices of firms. We presented our survey results to two different groups of practitioners comprising of business executives and senior investment bankers and consider their feedback as a test of the validity of our main conclusions.

Both groups provided very similar comments and found our main results to be largely consistent with their intuition. They were comfortable with our conclusions about the importance of financial flexibility and earnings per share in capital structure choice. They also agreed that our results documenting the sensitivity of responses to size and PE ratios in section 3 appear reasonable. Neither group was surprised by the similarity of views between European and U.S. managers on most dimensions. They also agreed with our main conclusion that legal systems may not fully capture the influence of country-specific variables that are relevant in capital structure choice. Further, they also provided several examples based on their personal experience to illustrate how country-specific constraints could impact the capital structure choices of European firms even within a legal system. For example, the level of technical difficulties to issue equity may differ significantly between countries within the same legal system.¹⁸

Both groups also cautioned us that the higher valuation of financial flexibility in our survey relative to that in GH study could be explained partly by the timing of our survey which was conducted immediately after September 11, 2001. Since this was a period of high uncertainty and low market liquidity, it may have introduced a bias toward higher valuation of financial flexibility by respondents. To examine whether the magnitude of the September 11 event bias varies among our survey respondents, we compared the responses received until December 2001 with those received after the third mailing in February 2002. We would expect that this bias would be much stronger in responses received immediately after September 11 relative to those in the second group. Our general conclusions are largely similar in both groups. Nonetheless, we do acknowledge that such a bias could be present in our data and caution the reader to keep this caveat in mind when drawing inferences pertaining to financial flexibility.

Overall, the comments of both groups on our survey results have increased confidence in our main findings and have helped us to improve our understanding of survey results.¹⁹

B.2. Nonresponse Bias

As discussed in Section 2 (Table II), both univariate and multinomial tests support that the proportions of our respondents across countries is similar to that in our initial sample to whom the survey was mailed. In this section, we examine whether characteristics of our respondents are also similar to that in our initial sample. We refer to our initial sample of 707 firms as our population firms since our results are generalizable only to similar population of European firms. We examine three such firm characteristics that are likely to be strongly associated with a firm's capital structure decision: market capitalization, PE ratios, and dividend policy. The population data are collected from the Bloomberg data base for the year ending December 2001.

These comparisons are reported in Table XVIII. The mean (median) market capitalization and P/E ratios of respondents are very similar to that of population firms across all legal systems.

The proportions of respondent firms that pay dividend is also similar to that in population across all legal systems except in the case of Scandinavian law countries.²⁰ Thus, nonresponse bias does not appear to be a major problem in our survey based on these characteristics.

In summary, our robustness checks provide us some reassurance as well as some caveats about our results. It is reassuring to find that two groups of practitioners from the field find that our main conclusions are consistent with their beliefs and that the differences in responses across legal systems are not conditional on firm or industry characteristics. Anecdotal evidence by practitioners as well as the pronounced differences in the responses of Scandinavian respondents relative to their other European counterparts on several dimensions, on the other hand, suggest that country-specific factors may also play a major role in the capital structure choices of firms. The timing of our survey around September 11 could have introduced some bias in responses that may affect our results on comparisons of the European managerial responses with those of the U.S. managers in the GH study. The reader should keep these caveats in mind when drawing inferences from our analysis.

5. Summary and Conclusions

We can draw several important conclusions from our survey of European managers. Two main considerations seem to influence the capital structure decisions of European managers: the search for financial flexibility and the impacts on the financial statements.

Financial flexibility is a key issue for managers to have access to external financing whatever the economic outlook. This financial flexibility is obtained by selecting the timing of the issue based on interest rate levels or market value of equity. This evidence is consistent with the window of opportunity hypothesis discussed in the literature. Our survey also confirms that managers are concerned about the impact of their decisions on financial statements. The concern

about earnings per share dilution is rated as an important concern in issuing common stock and is valued as a major advantage in issuing convertible debt. Credit rating and target ratios are also important issues for managers, which means that managers are very sensitive to external bearings. The weighted average cost of capital and tax advantage of debt are also important for managers, but these factors do not appear to drive the capital structure policies of European firms. While the cost of financing is a concern for managers, it does not seem to be a first level constraint relative to financial flexibility. Our results support the conclusion of Titman (2001): “Corporate treasurers do occasionally think about the kind of tradeoffs between tax savings and financial distress costs that we teach in our corporate finance classes. However, since this tradeoff does not change much over time, the balancing of the costs and benefits of debt financing that we emphasize so much in our textbooks is not their major concern. They spend much more thinking about changes in market conditions and the implications of these changes on how firms should be financed”.

Finally, we find little evidence that firms follow industry norms of capital structure or that managers use debt or equity for agency costs or tactical reasons such as to pressure employees or to motivate managers to work harder. We find moderate support for the trade-off theory but less for the pecking order theory.

Our comparative analysis of responses across countries with different legal systems provides some interesting findings. We find that major determinants of the capital structure choice are similar across European and US managers. However, this apparent similarity is somewhat misleading because we also discover substantial differences in responses across English, French, German, and Scandinavian law countries that cannot be explained by the quality of legal environment only. For example, the responses on debt and equity policy are very similar between French and German law countries with different quality of legal environment. Further, the managerial responses in the Scandinavian law countries are very different from their other European counterparts on many

dimensions while the managerial views in the English law countries are different to those in the US sample (also a common law country) in GH (2001) study on many dimensions. These differences do not appear to be driven by firm-specific or industry-specific factors.

In a previous study, Rajan and Zingales (1995) compare leverage across G-7 countries with carefully calculated detailed and more comparable measures and find remarkable similarities in the leverage as well as in correlations of leverage with different factors such as size and profitability across countries. However, a more indepth analysis reveals some inconsistencies that are puzzling. For example, they find a significant negative correlation between size and leverage in some countries contrary to the prediction of the theory. They conclude “this suggests that either our understanding of the economic underpinnings of the factors (e.g., that size is an inverse proxy for the expected costs of bankruptcy) or our understanding of the influence of the institutions (e.g., bankruptcy law), or both is flawed. More research is clearly called for.” Despite the limitations of survey methodology, our evidence supports similar conclusions. A lack of consistent patterns across different legal system countries as well as somewhat puzzling findings on some dimensions in our study suggest that the capital structure choice may be a consequence of complex interaction of many institutional features such as tax code, bankruptcy laws, and stock market development that is not fully captured by the legal system of a country. An indepth analysis of these issues is beyond the scope of this paper and is left for future research.

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Footnotes

¹ These include the trade-off theory, the pecking order theory, agency cost theory, and signaling information theory. See for example, Scott (1977), Miller (1977), Myers and Majluf (1984), Myers (1984), Ross (1977), Leland and Pyle (1977), Bradley et al. (1984), Jensen (1986), Kale et al. (1992), Barclay and Smith (1995), Jung et al. (1996), Graham (1996), Opler and Titman (1998), Sunder and Myers (1999), Titman and Wessels (1998), and Graham and Harvey (2001) for a review of capital structure literature.

² See for example, Harris and Raviv (1991), Titman (2001) and Welch (2002).

³ Other studies include Demircuc-Kent and Maksimovic (1996, 1999), Kester (1986), Mayer (1990), Remmers et al. (1974), Rutherford (1988), Stonehill et al. (1975), and Toy et al. (1974).

⁴ See for example, Eiteman, Stonehill, and Moffet (1998, page 8).

⁵ Pagano et al. (1999) show that there are significant differences in the characteristics of foreign listed and domestic listed European firms, especially in their debt to equity ratio, growth, and capital raising needs.

⁶ Graham and Harvey indicate that 26% of their sample firms have annual sales of less than 100 million USD and 42% have sales of over 1 billion USD. These percentages are 5% and 70% respectively in our sample based on annual sales in euro.

⁷ Data have been provided by BNP Paribas. The survey was mailed to the Chief Executive Officer (CEO) when the name of the CFO were not available.

⁸ The response rate of Graham and Harvey' study was 9%.

⁹ We adopt the Modigliani and Miller definition of Financial flexibility. As they stated in their 1963 paper, "the need for preserving flexibility will normally imply the maintenance by the corporation of a substantial reserve of untapped borrowing power" (p. 442). See Korajczyk, Lucas, and McDonald (1991), and Bayless and Chaplinsky (1996) for tests of window of opportunity hypothesis.

¹⁰ This factor and financial flexibility are also considered more important by firms with higher percentage of foreign sales. Some managers explained that it is really important to "negotiate financing when you don't need it".

¹¹ Bancel and Mittoo (2001) show that increase in prestige and visibility, and in number of shareholders are perceived as the major benefits by European managers.

¹² Alternatively, it can be viewed as consistent with the notion of financial flexibility supported in issuing debt.

¹³ For example, Ruthford (1988) shows that aggregate debt levels are higher for firms in Japan, France, and Germany than in the U.S. and U.K. Other studies include Demircuc-Kent and Maksimovic (1996, 1999), Kester (1986), Mayer (1990), Remmers et al. (1974), Stonehill et al. (1975), and Toy et al. (1974), Borio (1990) and Frankel and Montgomery (1991).

¹⁴ One possible explanation for the differences could be that the term financial flexibility is more open ended in our survey but is more tightly specified in the GH (2001) questionnaire.

¹⁵ The commonality of managerial responses in GH and our study irrespective of the differences in the strength of demographic correlations also indicates that there could be some other common determinants of the capital structure choice that need to be investigated in future.

¹⁶ There are differences across other legal systems also but these are fewer and are much less pronounced.

¹⁷ See for example, Heston and Rouwenhorst (1994) for evidence on differences in industrial structures among European countries.

¹⁸ Regarding issuing equity, the legal framework is quite homogeneous in Europe. But some practical aspects concerning market rules, placement modalities, determination of issuing price, etc. differ across Europe, which may induce difficulties to issue at certain periods of time. For example, in France, firms must issue at a price at least equal to an average computed with ten daily stock prices taken on the last twenty daily stocks prices before issuing (“rules of 10 among the 20”). This may induce a significant problem in case of decreasing stock prices (the only alternative would then be for the firm to issue with pre-emptive rights). Other example: “Equity line” programs are not allowed in all European countries, or may be accepted by Market authorities with strong constraints. These programs consist in dividing an equity issue into several periods of time and reserved it to a financial institution (with the admitted goal to sell these new shares to investors).

¹⁹ Very interesting issues have emerged when we presented our results to executives and senior bankers. These issues were not initially integrated in our questionnaire and would also have deserved an indepth analysis: the key role played by investment banks that influences firms financial policy, the appetite of investors for certain financial products at certain periods of time and the necessity for firms to adapt their financing policies to “fashion” and the past trajectories for of CFOs, success or failures that have an impact on their decisions. All these issues and opinions haven’t been tested in our questionnaire and are open for future research.

²⁰ We also conduct comparisons across countries wherever possible. The countries with fewer than five responses are combined for the test purposes. The cross-country results are largely similar to that reported for the legal systems.

Table I
Description of the Population Firms by Country of Origin

Country of Origin	Number of firms	Market Capitalization			Sales 2001		
		Average (Mil €)	Median (Mil €)	St. Dev.	Average (Mil €)	Median (Mil €)	St. Dev.
Austria	18	1,070.8	456.8	1,215.4	1,797.5	1,189.0	1,867.5
Belgium	21	4,535.7	969.7	5,589.8	6,145.4	2,204.0	6,712.5
Denmark	26	2,709.5	1,505.4	3,662.2	1,638.9	946.5	1,463.8
Finland	26	7,119.8	665.1	25,820.2	3,552.3	948.0	6,632.3
France	112	9,485.6	2,773.4	17,261.2	10,049.7	4,064.2	25,033.4
Germany	93	9,046.3	2,112.0	16,616.8	12,822.0	2,445.5	17,247.6
Greece	29	1,256.5	449.1	1,559.1	4,774.7	339.0	18,647.5
Ireland	12	5,655.8	3,346.9	4,831.2	2,616.1	1,376.0	2,608.1
Italy	59	7,079.8	2,787.1	10,353.1	7,752.3	2,408.0	12,962.7
Norway	30	970.3	335.7	2,271.4	5,329.8	480.5	20,241.9
Portugal	14	3,571.7	1,864.4	3,819.1	2,494.6	1,389.1	1,868.4
Spain	47	7,407.3	2,026.6	14,465.5	4,687.0	1,835.2	8,748.2
Sweden	22	7,989.7	5,337.9	12,581.9	7,042.8	4,625.5	6,950.7
Switzerland	25	19,475.7	5,818.3	27,585.2	7,383.0	3,770.0	8,238.5
The Netherlands	38	11,143.2	3,393.8	15,515.5	8,638.6	4,294.1	14,209.6
United Kingdom	135	15,100.2	5,364.4	32,085.5	9,215.4	4,434.0	18,843.9
Total	707	9,009.5	2,657.6	19,889.6	8,025.5	2,317.9	16,942.0

Table II
Tests of Nonresponse Bias across Legal Systems and Country of Origin

Legal System of the Country of Origin^a	No. of Sample Firms	Percentage of Sample Firms	Percentage of Respondents	P-value^b
French Law Countries	320	45.26%	45.98%	0.91 (0.15)
France	112	35.0%	32.5%	0.86
Belgium	21	6.56%	2.5%	0.49
Greece	29	9.06%	12.5%	0.56
Italy	59	18.44%	10.00%	0.27
Portugal	14	4.37%	12.5%	0.047*
Spain	47	14.69%	17.5%	0.64
The Netherlands	38	11.87%	12.5%	0.80
German Law Countries	136	19.24%	24.14%	0.32 (0.88)
Germany	93	68.38%	71.43%	0.81
Austria	18	13.23%	9.52%	0.75
Switzerland	25	18.38%	19.05%	0.99
Scandinavian Law	104	14.71%	16.09%	0.75 (0.45)
Denmark	26	25.0%	35.71%	0.52
Finland	26	25.0%	35.71%	0.52
Norway	30	28.85%	14.29%	0.35
Sweden	22	21.15%	14.29%	0.73
English Law Countries	147	20.79%	13.79%	0.16 (0.28)
United Kingdom	135	91.87%	83.33%	0.29
Ireland	12	8.16%	16.67%	0.29
Total	707	100.00%	100.00%	0.35

a. Based on La Porta etc (1997).

b. The p-values are computed using the Fisher's Exact Test for testing that the proportion of respondent firms in each country or in each Legal system is the same as in the population.

c. The p-values in parentheses are computed using the multinomial (Chi-square) test that the proportions of respondent firms across countries within each legal system proportions of respondent firms across countries within each legal system are the same as in the population (707 firms). The value in the last row and column (0.35) is the p-value for the multinomial test that the proportions of respondent firms across diiferent Legal systems are the same as in the population ie. 0.4526, 0.1924, 0.1471, and 0.2079 respectively.

Table III

Survey response to the question: What factors affect how you choose the appropriate amount of debt for your firm?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). We present the following variables: Size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firms have P/E ratio>14), industry (manufacturing includes manufacturing, energy and transportation sectors), Foreign List (firms listed on foreign exchanges) and Foreign Sales (percentage of total sales in foreign countries). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	Size		P/E		Industry		Foreign List		Foreign Sales	
			Small	Large	Growth	Non-G	Manu.	Others	Yes	No	<25%	>25%
g) Financial flexibility	90.8	3.39	3.43	3.32	3.42	3.26	3.50	3.36	3.36	3.45	3.06	3.46**
d) Our credit rating (as assigned by rating agencies)	73.17	2.78	2.34	3.5***	2.96	2.64	3.00	2.73	3.17	2.40***	2.25	2.90
a) The tax advantage of interest deductibility	58.14	2.59	2.42	2.74	2.74	2.22	2.72	2.56	2.75	2.42	2.17	2.69
m) The volatility of our earnings and cashflows	50.00	2.33	2.53	1.9**	2.21	2.09	2.13	2.38	2.28	2.34	2.00	2.45
e) The transactions costs and fees for issuing debt	33.33	1.94	1.86	1.94	2.07	1.47*	2.06	1.91	1.78	2.02	1.94	1.94
h) We limit debt so our customers/suppliers are not worried about our financial stability	32.56	1.97	2.04	1.93	2.02	1.96	1.94	1.97	1.89	1.98	1.83	1.97
b) The potential costs of bankruptcy or near bankruptcy financial distress	30.95	1.76	2.00	1.37**	1.45	2.04	1.44	1.85	1.51	1.89	1.64	1.79
c) The debt levels of other firms in our industry	23.26	1.84	1.68	2.13**	1.67	2.00	1.78	1.85	2.1	1.67*	1.78	1.84
f) The personal tax cost that our investors face when they receive interest income	10.59	0.96	0.90	0.93	1.07	0.69	1.00	0.96	1.06	0.82	1.06	0.92
l) To ensure that upper management works hard and efficiently	6.98	0.73	0.90	0.39*	0.74	0.91	0.59	0.77	0.64	0.84	0.83	0.69
i) We try to have enough debt so that we are not an attractive target	4.65	0.85	0.92	0.77	0.88	0.83	0.94	0.83	0.89	0.87	0.94	0.80
j) If we issue debt our competitors know that we are very unlikely to reduce our output	1.16	0.44	0.46	0.45	0.51	0.51	0.40	0.45	0.47	0.40	0.39	0.44
k) A high debt ratio helps us bargain for concessions from our employees	0.00	0.27	0.32	0.16	0.30	0.17	0.18	0.29	0.22	0.31	0.28	0.27

Table IV

Survey response to the question: What other factors affect your firm's debt policy?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). We present the following variables: Size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firms have P/E ratio>14), industry (manufacturing includes manufacturing, energy and transportation sectors), Foreign List (firms listed on foreign exchanges) and Foreign Sales (percentage of total sales in foreign countries). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	Size		P/E		Industry		Foreign List		Foreign Sales	
			Small	Large	Growth	Non-G	Manu.	Others	Yes	No	<25%	>25%
i) With the use of debt, we try to minimise the weighted average cost of capital	69.77	2.80	2.74	2.71	2.72	2.65	2.82	2.80	2.86	2.64	3.06	2.72
c) We issue debt when interest rates are low	44.83	2.10	2.11	2.00	2.05	1.91	2.17	2.08	1.94	2.17	2.11	2.05
d) We use debt when our equity is undervalued by the market	43.68	2.08	2.04	1.97	1.95	2.04	1.89	2.13	2.22	1.91	1.89	2.17
a) We issue debt when our recent profits are not sufficient to fund our activities	24.14	1.56	1.84	1.06***	1.44	1.39	1.44	1.59	1.47	1.54	1.50	1.57
b) Using debt gives investors a better impression of our firm's prospects that issuing stocks	20.00	1.55	1.65	1.41	1.57	1.55	1.5	1.57	1.65	1.48	1.44	1.56
g) Changes in the price of our common stock	15.12	1.34	0.03	1.13	1.3	0.91*	1.24	1.36	1.33	1.24	1.11	1.41
j) We prefer banks to bonds because it avoids our firm to disclose too much information	14.12	1.02	1.32	0.53***	1.05	0.96	0.88	1.06	0.80	1.24	0.94	1.10
f) We delay issuing or retiring debt because of transactions costs and fees	5.81	0.92	1.14	0.71**	1.00	0.74	0.71	1.07	0.89	1.04	0.94	1.00
e) We use debt because of our close relationship with a bank (house bank)	3.49	0.73	0.86	0.53	0.69	0.87	0.44	0.81	0.69	0.83	0.53	0.80
h) We issue debt when we have accumulated profits	1.18	0.72	0.70	0.73	0.79	0.52	0.47	0.78	0.71	0.76	0.77	0.68

Table V

Survey Response to the question: What factors affect your firm's choice between short- and long-term debt?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). We present the following variables: Size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firms have P/E ratio>14), industry (manufacturing includes manufacturing, energy and transportation sectors), Foreign List (firms listed on foreign exchanges) and Foreign Sales (percentage of total sales in foreign countries). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	Size		P/E		Industry		Foreign List		Foreign Sales	
			Small	Large	Growth	Non-G	Manu.	Others	Yes	No	<25%	>25%
b) Matching the maturity of our debt with the life of our assets	77.01	3.10	3.08	3.16	2.95	3.39*	3.39	3.03	3.06	3.07	3.39	3.00*
f) We issue long-term debt to minimize the risk of having to finance in “bad times”	69.77	2.83	2.8	2.74	2.58	2.96	3.00	2.78	2.82	2.78	2.22	2.95**
a) We issue short term when we are waiting for long term market interest rates to decline	31.03	1.85	1.86	1.81	1.93	1.57	1.94	1.83	1.64	1.91	2.00	1.80
d) We expect our rating to improve, so we borrow short term until it does	7.14	0.90	0.90	0.90	1.07	0.55**	0.88	0.91	0.97	0.81	0.82	0.94
c) We borrow short-term so that returns from new projects can be captured by shareholders	5.75	1.02	1.14	0.74**	1.12	0.78*	1.17	0.99	1.04	0.87	1.11	1.05
e) Borrowing short-term reduces the chance that our firm will want to take on risky projects	1.16	0.53	0.68	0.29***	0.58	0.48	0.47	0.55	0.36	0.67**	0.72	0.52

Table VI

Survey response to the question: Has your firm seriously considered issuing common stock?

If yes, what factors affect your firm's decisions about issuing common stock?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). We present the following variables: Size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firms have P/E ratio>14), industry (manufacturing includes manufacturing, energy and transportation sectors), Foreign List (firms listed on foreign exchanges) and Foreign Sales (percentage of total sales in foreign countries). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	Size		P/E		Industry		Foreign List		Foreign Sales	
			Small	Large	Growth	Non-G	Manu.	Others	Yes	No	<25%	>25%
m) Earning per share dilution	66.04	2.72	2.39	3.15**	2.77	2.27	2.27	2.50	2.88	2.48	2.89	2.66
e) Maintaining a target debt-to-equity ratio	59.26	2.67	2.54	2.67	2.45	2.67	3.13	2.59	2.84	2.48	2.30	2.69
a) If our stock price has recently risen, the price at which we can issue is "high"	59.26	2.61	2.64	2.62	2.68	2.25	2.50	2.63	2.64	2.56	2.90	2.50
k) The amount by which our stock is undervalued or overvalued by the market	53.7	2.44	2.32	2.57	2.45	2.08	2.70	2.39	2.52	2.36	2.39	2.45
c) Providing shares to employee stock option plan	44.44	2.07	1.75	2.10	2.10	1.00**	2.67	1.96*	1.96	2.16	2.00	2.00
g) Whether our recent profits have been sufficient to fund our activities	32.08	1.94	1.93	1.95	1.97	2.00	1.63	2.00	1.79	2.20	2.40	1.85
j) Diluting the holdings of certain shareholders	29.63	1.67	1.46	1.71	1.77	0.75**	2.75	1.48*	1.44	1.76	1.20	1.79
f) Using a similar debt/equity ratio as is used by other firms in our industry	27.78	1.85	1.71	2.05	1.68	1.92	1.50	1.91	2.16	1.64*	1.60	1.88
b) Stock is our "least risky" source of funds	25.93	1.50	1.61	1.38	1.68	1.00*	1.63	1.48	1.72	1.32	1.89	1.38
n) In case of paying a target by shares, the ability to use the pooling of interest method	22.00	1.56	1.44	1.55	1.6	0.80	1.25	1.62	1.39	1.65	1.67	1.46
h) Issuing stock gives a better impression of our firm's prospects than using debt	9.06	1.15	1.25	1.00	1.32	0.58***	0.63	1.24	1.28	1.04	1.50	1.02
i) The capital gains tax rates faced by our investors (relative to tax rates on dividends)	7.41	0.98	0.93	0.90	1.19	0.33***	0.38	1.09**	0.84	1.08	1.20	0.90
d) Common stock is our cheapest source of funds	7.41	0.67	0.71	0.62	0.81	0.17***	0.75	0.65	0.76	0.64	0.70	0.57
l) Inability to obtain funds using other sources	5.56	0.93	1.11	0.48***	0.68	0.83	1.25	0.87	0.72	1.00	0.84	0.93

Table VII
Survey response to the question: Has your firm seriously considered issuing convertible debt (or issued debt in last ten years)?
If yes, what factors affect your firm's decisions about issuing convertible debt?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). We present the following variables: Size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firms have P/E ratio >14), industry (manufacturing includes manufacturing, energy and transportation sectors), Foreign List (firms listed on foreign exchanges) and Foreign Sales (percentage of total sales in foreign countries). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	Size		P/E		Industry		Foreign List		Foreign Sales	
			Small	Large	Growth	Non-G	Manu.	Others	Yes	No	<25%	>25%
a) Convertibles are an inexpensive way to issue "delayed" common stock	57.14	2.45	2.13	2.94**	2.35	2.50	3.17	2.33**	2.71	2.07*	2.40	2.42
g) Ability to "call" or force conversion of convertible debt if/when we need to	54.76	2.43	2.43	2.41	2.42	2.75	2.50	2.42	2.42	2.47	2.17	2.46
f) Our stock is currently undervalued	51.16	2.40	2.67	2.00**	2.38	2.25	2.50	2.38	2.21	2.56	2.67	2.33
e) Avoiding short-term equity dilution	51.16	2.16	2.42	2.00	2.67	1.63*	2.00	2.19	2.13	2.25	3.00	2.08*
c) Convertibles are less expensive than debt	35.71	1.86	1.70	2.12	1.70	1.63	2.00	1.83	1.96	1.60	2.40	1.72
h) To attract investors unsure about the riskiness of our firm	26.83	1.68	1.77	1.59	1.61	1.75	1.90	1.67	1.61	1.80	1.50	1.65
d) Other firms in our industry successfully use convertibles	18.60	1.09	1.04	1.29	1.00	1.13	0.50	1.19	1.33	0.81	1.50	0.94
b) Protecting bondholders against unfavourable actions by managers or stockholders	4.65	0.88	1.00	0.76	0.88	0.63	0.33	0.97**	0.88	1.06	1.50	0.75

Table VIII

Survey response to the question: Has your firm seriously considered issuing (or issued) common stock or debt in foreign countries in the last decade? If yes, what factors affect your firm's decisions about issuing in foreign markets?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). We present the following variables: Size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firms have P/E ratio>14), industry (manufacturing includes manufacturing, energy and transportation sectors), Foreign List (firms listed on foreign exchanges) and Foreign Sales (percentage of total sales in foreign countries). ***,**,* denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	Size		P/E		Industry		Foreign List		Foreign Sales	
			Small	Large	Growth	Non-G	Manu.	Others	Yes	No	<25%	>25%
b) keeping the "source of funds" close to its "use"	67.35	2.71	2.83	2.61	2.60	3.00	1.75	2.90**	2.63	2.70	3.30	2.55
c) Providing a "natural hedge"	66.67	2.69	2.74	2.52	2.48	2.90	2.38	2.75	2.63	2.63	2.57	2.64
a) Favorable tax treatment relative to Europe	52.08	2.06	2.38	1.53*	2.00	1.70	1.88	2.10	1.58	2.7***	1.71	2.05
f) Market conditions may be better than domestic conditions	44.90	2.08	1.96	2.21	2.13	1.60	1.75	2.15	2.04	2.30	2.43	2.03
d) Lower interest rates in foreign markets	26.09	1.48	1.59	1.36	1.64	0.70**	1.13	1.55	1.42	1.67	1.29	1.46
e) Foreign regulations require us to issue abroad	20.83	1.23	1.39	1.09	1.17	1.00	1.13	1.25	1.33	1.16	0.86	1.28

Table IX

Survey response to the question: What factors affect how you choose the appropriate amount of debt for your firm?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	US		European Countries				Univariate T-test for Difference in Means (P-value)					
			ALL	Fortune 500	English Law	French Law	German Law	Scandinavian Law	English Law = French Law	English Law = German law	English Law = Scand. Law	French Law = German Law	French Law = Scand. Law	German Law = Scand. Law
g) Financial flexibility	90.80	3.39	2.59	2.55	3.00	3.48	3.43	3.43	0.03**	0.07*	0.09*	0.80	0.82	1.00
d) Our credit rating (as assigned by rating agencies)	73.17	2.78	2.46	3.31	2.58	2.58	3.14	2.92	1.00	0.22	0.54	0.055*	0.45	0.61
a) The tax advantage of interest deductibility	58.14	2.59	2.07	2.53	2.92	2.87	2.33	1.93	0.09*	0.15	0.015**	0.10*	0.005***	0.27
m) The volatility of our earnings and cashflows	50.00	2.33	2.32	2.30	2.00	2.42	2.3	2.42	0.28	0.47	0.44	0.70	0.99	0.81
e) The transactions costs and fees for issuing debt	33.33	1.94	1.95	1.70	1.41	2.05	2.29	1.57	0.13	0.07*	0.76	0.48	0.21	0.13
h) We limit debt so our customers/suppliers are not worried about our financial stability	32.56	1.97	1.24	0.98	1.17	2.18	2.10	1.86	0.012**	0.024**	0.11	0.78	0.33	0.47
b) The potential costs of bankruptcy or near bankruptcy financial distress	30.95	1.76	1.24	1.08	1.58	1.87	1.35	2.23	0.55	0.64	0.23	0.14	0.37	0.044**
c) The debt levels of other firms in our industry	23.26	1.84	1.49	1.86	1.67	1.85	1.9	1.86	0.6	0.54	0.6	0.85	0.98	0.88
f) The personal tax cost that our investors face when they receive interest income	10.59	0.96	0.68	0.72	0.50	1.11	1.19	0.64	0.06*	0.05*	0.7	0.75	0.13	0.11
l) To ensure that upper management works hard and efficiently	6.98	0.73	0.33	0.17	0.83	0.75	0.67	0.69	0.77	0.58	0.71	0.72	0.80	0.94
i) We try to have enough debt so that we are not an attractive target	4.65	0.85	0.73	0.88	0.75	0.85	0.86	0.92	0.75	0.76	0.66	0.98	0.93	0.85
j) If we issue debt our competitors know that we are very unlikely to reduce our output	1.16	0.44	0.40	0.36	0.17	0.55	0.52	0.23	0.024**	0.10*	0.70	0.90	0.07*	0.18
k) A high debt ratio helps us bargain for concessions from our employees	0.00	0.27	0.16	0.14	0.25	0.25	0.43	0.08	1.00	0.34	0.27	0.24	0.10	0.03**

Table X
Survey Response to the question: What factors affect your firm's choice between short- and long-term debt?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	US		European Countries				Univariate T-test for Difference in Means (P-value)					
			ALL	Fortune 500	English Law	French Law	German Law	Scandinavian Law	English Law = French Law	English Law = German law	English Law = Scand. Law	French Law = German Law	French Law = Scand. Law	German Law = Scand. Law
b) Matching the maturity of our debt with the life of our assets	77.01	3.10	2.60	2.39	2.48	3.43	3.19	2.93	0.0013**	0.006***	0.058*	0.31	0.14	0.45
f) We issue long-term debt to minimize the risk of having to finance in "bad times"	69.77	2.83	2.15	2.31	2.42	2.95	2.76	2.92	0.17	0.38	0.33	0.44	0.06*	0.71
a) We issue short term when we are waiting for long term market interest rates to decline	31.03	1.85	1.78	1.94	1.00	1.80	2.52	1.71	0.014**	0.0001***	0.041**	0.021**	0.76	0.02**
c) We borrow short-term so that returns from new projects can be captured by shareholders	5.75	1.02	0.94	0.70	0.75	1.08	1.10	1.00	0.27	0.3	0.37	0.94	0.67	0.68
d) We expect our rating to improve, so we borrow short term until it does	7.14	0.90	0.85	0.70	0.75	0.87	1.10	0.83	0.70	0.36	0.85	0.43	0.92	0.53
e) Borrowing short-term reduces the chance that our firm will want to take on risky projects	1.16	0.53	0.53	0.29	0.17	0.65	0.57	0.46	0.006***	0.004***	0.19	0.68	0.40	0.64

Table XI
Survey response to the question: What other factors affect your firm's debt policy?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	US		European Countries				Univariate T-test for Difference in Means (P-value)					
			ALL	Fortune 500	English Law	French Law	German Law	Scandinavian Law	English Law = French Law	English Law = German Law	English Law = Scand. Law	French Law = German Law	French Law = Scand. Law	German Law = Scand. Law
i) With the use of debt, we try to minimise the weighted average cost of capital	69.77	2.8	NA	NA	2.33	3.00	2.81	2.62	0.14	0.31	0.60	0.50	0.33	0.65
c) We issue debt when interest rates are low	44.83	2.10	2.22	2.35	1.17	2.15	2.62	2.00	0.02**	0.002***	0.08*	0.13	0.68	0.13
d) We use debt when our equity is undervalued by the market	43.68	2.08	1.56	1.67	1.92	2.23	1.86	2.14	0.44	0.89	0.62	0.23	0.82	0.45
a) We issue debt when our recent profits are not sufficient to fund our activities	24.14	1.56	2.13	1.75	1.00	1.80	1.57	1.36	0.06*	0.19	0.45	0.45	0.22	0.59
b) Using debt gives investors a better impression of our firm's prospects that issuing stocks	20.0	1.55	0.96	1.14	1.30	1.83	1.24	1.43	0.19	0.87	0.76	0.025**	0.22	0.54
g) Changes in the price of our common stock	15.12	1.34	1.08	1.10	1.08	1.43	1.33	1.31	0.35	0.51	0.61	0.73	0.74	0.94
j) We prefer banks to bonds because it avoids our firm to disclose too much information	14.12	1.02	NA	NA	0.91	1.13	1.00	0.85	0.64	0.85	0.91	0.69	0.51	0.74
f) We delay issuing or retiring debt because of transactions costs and fees	5.81	0.92	1.04	0.89	1.33	1.03	0.71	1.13	0.47	0.18	0.61	0.16	0.87	0.30
e) We use debt because of our close relationship with a bank (house bank)	3.49	0.73	NA	NA	0.92	0.64	0.48	1.21	0.48	0.28	0.51	0.43	0.06*	0.03**
h) We issue debt when we have accumulated profits	1.18	0.72	0.53	0.55	0.91	0.73	0.62	0.69	0.45	0.50	0.62	0.56	0.87	0.75

Table XII
Survey response to the question: Has your firm seriously considered issuing common stock?
If yes, what factors affect your firm's decisions about issuing common stock?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	US		European Countries				Univariate T-test for Difference in Means (P-value)					
			ALL	Fortune 500	English Law	French Law	German Law	Scandinavian Law	English Law = French Law	English Law = German law	English Law = Scand. Law	French Law = German Law	French Law = Scand. Law	German Law = Scand. Law
m) Earning per share dilution	66.04	2.72	2.84	3.29	3.2	2.96	2.87	1.56	0.45	0.37	0.003***	0.82	0.007***	0.02**
e) Maintaining a target debt-to-equity ratio	59.26	2.67	2.26	2.38	1.40	2.8	2.73	2.89	0.02**	0.026**	0.03**	0.80	0.86	0.77
a) If our stock price has recently risen, the price at which we can issue is "high"	59.26	2.61	2.53	2.79	2.60	2.88	2.53	2.00	0.64	0.91	0.33	0.37	0.02**	0.15
k) The amount by which our stock is undervalued or overvalued by the market	53.7	2.44	2.69	2.43	3.20	2.44	2.40	2.11	0.13	0.11	0.08*	0.91	0.52	0.56
c) Providing shares to employee stock option plan	44.44	2.07	2.34	2.74	1.50	2.11	2.40	2.11	0.43	0.28	0.85	0.54	0.51	0.32
g) Whether our recent profits have been sufficient to fund our activities	32.08	1.94	1.76	1.22	1.00	2.00	2.21	1.89	0.09*	0.06*	0.15	0.58	0.78	0.51
j) Diluting the holdings of certain shareholders	29.63	1.67	2.14	1.65	1.00	1.76	1.80	1.56	0.32	0.3	0.52	0.93	0.75	0.71
f) Using a similar debt/equity ratio as is used by other firms in our industry	27.78	1.85	1.45	1.3	1.40	1.84	2.13	1.67	0.37	0.17	0.63	0.43	0.67	0.30
b) Stock is our "least risky" source of funds	25.93	1.5	1.76	1.17	2.40	1.72	1.13	1.00	0.39	0.14	0.11	0.09*	0.07*	0.73
n) In case of paying a target by shares, the ability to use the pooling of interest method	22.00	1.56	NA	NA	0.80	1.52	2.14	1.13	0.43	0.18	0.74	0.14	0.47	0.10*
h) Issuing stock gives a better impression of our firm's prospects than using debt	9.06	1.15	1.31	0.91	1.40	1.16	1.13	1.00	0.68	0.66	0.52	0.94	0.66	0.73
i) The capital gains tax rates faced by our investors (relative to tax rates on dividends)	7.41	0.98	0.82	0.83	0.60	0.96	1.20	0.89	0.28	0.11	0.51	0.45	0.86	0.48
d) Common stock is our cheapest source of funds	7.41	0.67	1.10	0.52	1.00	0.80	0.60	0.22	0.82	0.64	0.38	0.48	0.04*	0.10*
l) Inability to obtain funds using other sources	5.56	0.93	1.15	0.91	0.80	1.00	0.73	1.11	0.65	0.88	0.59	0.38	0.82	0.40

Table XIII

**Survey response to the question: Has your firm seriously considered issuing convertible debt (or issued debt in last ten years)?
If yes, what factors affect your firm's decisions about issuing convertible debt?**

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). ***, **, * denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	US		European Countries				Univariate T-test for Difference in Means (P-value)					
			ALL	Fortune 500	English Law	French Law	German Law	Scandinavian Law	English Law = French Law	English Law = German law	English Law = Scand. Law	French Law = German Law	French Law = Scand. Law	German Law = Scand. Law
a) Convertibles are an inexpensive way to issue "delayed" common stock	57.14	2.45	2.49	2.41	2.67	2.67	2.5	1.20	1.00	0.83	0.16	0.65	0.06**	0.09*
g) Ability to "call" or force conversion of convertible debt if/when we need to	54.76	2.43	2.29	2.31	1.75	2.57	2.10	3.00	0.36	0.68	0.2	0.13	0.27	0.05**
f) Our stock is currently undervalued	51.16	2.4	2.34	2.47	2.25	2.46	2.3	2.40	0.85	0.97	0.90	0.66	0.90	0.85
e) Avoiding short-term equity dilution	51.16	2.16	2.18	2.59	2.75	2.33	2.22	0.80	0.29	0.26	0.004***	0.79	0.009***	0.02**
c) Convertibles are less expensive than debt	35.71	1.86	1.85	1.25	2.33	1.86	2.00	1.20	0.74	0.81	0.46	0.76	0.34	0.27
h) To attract investors unsure about the riskiness of our firm	26.83	1.68	2.07	1.75	1.00	1.69	1.50	2.75	0.41	0.56	0.09*	0.64	0.012**	0.013**
d) Other firms in our industry successfully use convertibles	18.6	1.09	1.10	0.80	1.00	1.08	1.00	1.67	0.92	1.00	1.00	0.85	0.53	0.46
b) Protecting bondholders against unfavourable actions by managers or stockholders	4.65	0.88	0.62	0.56	0.75	0.96	0.90	0.60	0.71	0.76	0.79	0.85	0.29	0.39

Table XIV

Survey response to the question: Has your firm seriously considered issuing (or issued) common stock or debt in foreign countries in the last decade? If yes, what factors affect your firm's decisions about issuing in foreign markets?

Respondents are asked to rate on a scale of 0 (not important) to 4 (very important). We report the overall mean as well as the % of respondents that answered 3 and 4 (important and very important). ***,**,* denotes a significant difference at the 1%, 5%, and 10% level, respectively.

	Important or very important (%)	Mean	US		European Countries				Univariate T-test for Difference in Means (P-value)					
			ALL	Fortune 500	English Law	French Law	German Law	Scandinavian Law	English Law = French Law	English Law = German Law	English Law = Scand. Law	French Law = German Law	French Law = Scand. Law	German Law = Scand. Law
b) keeping the "source of funds" close to its "use"	67.35	2.71	2.67	2.3	1.63	3.27	2.73	1.25	0.023**	0.12	0.67	0.18	0.043	0.09
c) Providing a "natural hedge"	66.67	2.69	3.15	3.00	1.63	3.24	2.64	1.50	0.014**	0.12	0.91	0.16	0.17	0.33
a) Favorable tax treatment relative to Europe	52.08	2.06	2.26	2.11	1.50	2.10	2.50	2.00	0.44	0.25	0.67	0.48	0.34	0.65
f) Market conditions may be better than domestic conditions	44.9	2.08	NA	NA	1.75	1.96	2.82	1.50	0.69	0.054*	0.76	0.054*	0.55	0.13
d) Lower interest rates in foreign markets	26.09	1.48	2.19	2.03	0.88	1.44	2.22	1.25	0.22	0.03**	0.55	0.15	0.74	0.17
e) Foreign regulations require us to issue abroad	20.83	1.23	0.63	0.62	1.75	0.92	1.28	2.00	0.29	0.56	0.86	0.41	0.42	0.58

Table XV
Correlations of Control variables from the Survey

Kendall's Tau, a measure of correlation between two ordinal-level (rankable) variables is reported. ***, **, * denote significant difference in means (medians) at the 1%, 5%, and 10% levels, respectively.

Panel A: size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firm has P/E ratio greater than 14), D/E (leveraged firm has debt to equity greater than 0.3), dividends (whether the firm pays dividends), rating (high has debt rated BBB or above), industry (manufacturing / energy / transportation versus all others), managerial stock ownership (high is greater than 5%), age (CEO older than 59 versus younger than 60), CEO tenure (long is nine or more years on the job), education (whether the CEO has an MBA), utility (whether the firm is regulated), equity (public versus private, family or government controlled corporations), foreign sales (whether foreign sales are greater than 25% of total sales), D/E (whether the firm reports a target debt ratio), foreign listing (whether listed on foreign stock exchanges or not).

Panel B: first five variables, inflshr, inflbond, inflemp, inflgovt, inflgovt, measure whether influence of shareholders, bondholders, employees, government, and local government respectively on financing decisions of the firm is high or low. Other Panel B variables include Multiple (multiple classes of shares or not), issuestk (shares issued in last ten years or not), freefloat (percentage of free float of shares is low (<50%)), eqcost (estimated cost of equity), and CAPM (use CAPM or not for estimating cost of equity).

	SIZE (Small to large)	P/E (low to high)	D/E (low to high)	Dividends (yes to no)	Rating (high to low)	Industry (manu. to p low)	Ownersh (high to low)	Age (young to mature)	Tenure (short to long)	Education (MBA to others)	Utility (yes to no)	Equity (public to private)	For. Rev (High to low)	Target D/E (no to yes)	FRNLST (no to yes)	Inflshr no<=2 (no to yes)	Inflbond (no to yes)	Inflemp (no to yes)	Inflgovt (no to yes)	Inflloco vt (no to yes)	Multiple (no to yes)	issuestk (no to yes)	freefloat< 50% (low to high)	eqcost<m edian 9.5 (low to high)
Panel A:																								
P/E	-0.24**																							
D/E	-0.08	-0.15																						
Dividends	-0.17	0.09	0.32**																					
Rating	0.17	-0.17	0.09	-0.11																				
Industry	-0.12	0.2	0.11	0	0.14																			
Ownership	-0.20*	0.26**	0.07	-0.09	-0.01	-0.07																		
Age	-0.06	0.02	0.08	-0.11	0.01	-0.02	-0.09																	
Tenure	0.03	0.05	-0.06	-0.05	-0.01	0.21	0.08	0.43***																
Education	-0.21*	-0.11	0.24*	-0.05	0.11	0.09	-0.05	0.18	0.08															
Utility	0.16	-0.09	-0.05	0.07	-0.02	-0.04	-0.03	0.011	-0.21*	-0.08														
Equity	0.018	0.06	0.14	-0.04	0.05	0.03	-0.03	0.1	0.24**	-0.18	-0.24**													
ForRev	0.21*	-0.01	-0.07	0.13	0.19*	-0.30**	-0.1	0.11	-0.08	0.003	0.27**	0.05												
Target D/E	-0.09	-0.23*	0.1	-0.03	0.09	-0.14	0.15	0.17	0.11	-0.02	0.01	-0.09	0.01											
FRNLST	0.46***	-0.02	0.07	0.04	0.06	-0.04	0.01	-0.1	-0.013	-0.08	0.11	-0.19*	0.22*	0.09										
Panel B:																								
Inflshr	0.09	0.03	0.1	0.07	-0.25	-0.09	-0.04	0.06	-0.03	0.16	0.11	0.07	0.12	0.03	0.1									
Inflbond	0.08	0.05	0.11	-0.1	0	0.13	-0.09	0.07	-0.013	0.02	-0.02	-0.08	0.03	-0.04	-0.11	0.05								
Inflemp	0.03	0.03	0.01	0.08	0	0.03	0.1	-0.15	-0.20*	0.09	0	0.08	0.03	-0.17	-0.04	0.15	0.17							
Inflgovt	-0.05	0.08	-0.13	-0.09	0.08	0.01	0.17	0.04	0.05	0.03	-0.05	0.11	-0.09	0.03	-0.03	-0.08	0.04	0.25**						
Infllocovt	-0.13	0.1	-0.22*	-0.06	0	-0.06	0.26*	-0.14	0	-0.22*	0.08	0.1	0.09	-0.21*	-0.03	-0.22**	-0.14	0.12	0.52***					
Multiple	0.12	-0.05	0.23*	-0.14	0.06	0.06	0.22	-0.25**	0	-0.36**	-0.11	0.28**	-0.03	0.08	0.08	0.03	0.04	0.01	0.1	0.07				
issuestk	0.13	0.36***	0.04	0.14	0.02	0.12	0.02	0.17	-0.014	-0.11	0.16	0.08	0.04	0.13	0.11	0.04	0.12	0.03	0.04	0.02	-0.27**			
freefloat	0.12	0.23*	-0.19	0.18	0.33*	-0.01	-0.03	0.02	-0.09	-0.014	0.19	-0.22*	0.21*	-0.01	0.09	-0.21**	0.05	-0.17	-0.21**	-0.22**	-0.12	-0.013		
eqcost	0.05	-0.22	0.22*	0.09	0.07	-0.17	-0.12	0.03	-0.21	0.17	0.01	-0.12	0.17	0.01	0.17	0.14	0.2	0.17	0	-0.08	-0.14	0.08	0.02	
capm	0.04	0.18	0.05	-0.05	-0.09	0.1	-0.11	0.11	0.05	0.21*	0.39***	-0.16	0.08	-0.08	-0.13	0.15	0.05	-0.08	0.09	0.12	-0.16	0.001	0.13	-0.23**

Table XVI
Comparisons of Firm Characteristics Across Different Legal System Countries

Panel A: size (large firms have market capitalization greater than 5,000 million euro), P/E (growth firm has P/E ratio greater than 14), D/E (leveraged firm has debt to equity greater than 0.3), dividends (whether the firm pays dividends), rating (high has debt rated BBB or above), industry (manufacturing / energy / transportation versus all others), managerial stock ownership (high is greater than 5%), age (CEO older than 59 versus younger than 60), CEO tenure (long is nine or more years on the job), education (whether the CEO has an MBA), utility (whether the firm is regulated), equity (public versus private, family or government controlled corporations), foreign sales (whether foreign sales are Panel B: first five variables, inflshr, inflbond, inflemp, inflgovt, infllgovt, measure whether influence of shareholders, bondholders, employees, government, and local government respectively on financing decisions of the firm is high or low. Other Panel B variables include Multiple (multiple classes of shares or not), issuestk (shares issued in last ten years or not), free float (percentage of free float of shares is low (<50%)), eqcost (estimated cost of equity), and CAPM (use CAPM or not for estimating cost of equity).

***, **, * denote significant difference in means (medians) at the 1%, 5%, and 10% levels, respectively.

	Mean (median)	European Countries Mean (median)				P-values for univariate T-test for Difference in Means and Wilcoxon test for difference in medians (in parentheses)					
		English Law	French Law	German Law	Scandi. Law	English Law = French Law	English Law = German law	English Law = Scandin. Law	French Law = German Law	French Law = Scandi. Law	German Law = Scandi. Law
Panel A:											
SIZE	11245.6 (2910)	18302 (5375)	10373.8 (2731)	8553.7 (1800)	11214.5 (1300)	0.29 (0.22)	0.25 (0.22)	0.56 (0.25)	0.72 (0.64)	0.90 (0.42)	0.71 (0.59)
P/E	19.43 (16)	22.5 (17)	19.3 (15.4)	18.4 (17.5)	17.86 (12.5)	0.44 (0.69)	0.41 (0.94)	0.48 (0.22)	0.74 (0.73)	0.71 (0.24)	0.89 (0.20)
D/E	0.44 (0.24)	0.31 (0.15)	0.62 (0.44)	0.41 (0.26)	0.18 (0.17)	0.14 (0.053*)	0.55 (0.45)	0.36 (0.92)	0.26 (0.26)	0.03** (0.03**)	0.13 (0.02**)
Dividends	0.95 (1.0)	0.89 (1.0)	0.92 (1.0)	1.0 (1.0)	1.0 (1.0)	0.76 (0.76)	0.14 (0.14)	0.22 (0.21)	0.23 (0.20)	0.16 (0.20)	0.01** (0.03**)
Rating	1.55 (0.0)	2.0 (0.5)	1.46 (0.0)	1.79 (0.0)	1.07 (0.0)	0.48 (0.47)	0.83 (0.65)	0.27 (0.47)	0.62 (0.83)	0.55 (0.93)	0.33 (0.77)
Industry	4.8 (5.0)	6.0 (6.5)	4.0 (5.0)	4.8 (4.0)	4.6 (4.5)	0.07* (0.07*)	0.16 (0.16)	0.13 (0.14)	0.74 (0.64)	0.97 (0.94)	0.82 (0.85)
Ownership	1.27 (1.0)	1.25 (1.0)	1.15 (1.0)	1.37 (1.0)	1.43 (1.0)	0.66 (0.75)	0.69 (0.43)	0.62 (0.41)	0.29 (0.12)	0.22 (0.12)	0.84 (0.74)
Age	2.94 (3.0)	2.9 (3.0)	3.0 (3.0)	3.05 (3.0)	2.57 (3.0)	0.65 (0.53)	0.48 (0.47)	0.05* (0.05*)	0.90 (0.99)	0.06* (0.045**)	0.02** (0.03**)
Tenure	1.94 (2.0)	1.67 (2.0)	2.21 (2.0)	1.85 (2.0)	1.57 (1.0)	0.05* (0.04**)	0.54 (0.63)	0.75 (0.53)	0.13 (0.14)	0.02** (0.02**)	0.36 (0.33)
Education	2.5 (2.0)	2.1 (3.0)	2.5 (2.5)	2.76 (3.0)	2.46 (2.0)	0.24 (0.20)	0.14 (0.14)	0.35 (0.26)	0.42 (0.45)	0.23 (0.82)	0.40 (0.43)
Utility	0.08 (0.0)	0.0 (0.0)	0.14 (0.0)	0.06 (0.0)	0.0 (0.0)	0.28 (0.27)	0.52 (0.50)	NA (NA)	0.38 (0.30)	0.20 (0.20)	0.44 (0.43)
Equity	2.44 (2.0)	2.19 (2.0)	2.65 (2.0)	2.35 (2.0)	2.21 (2.0)	0.10 (0.12)	0.41 (0.45)	0.85 (0.84)	0.18 (0.25)	0.09 (0.12)	0.47 (0.54)
ForRev	3.23 (4.0)	3.65 (4.0)	2.89 (3.0)	3.38 (3.0)	3.5 (3.0)	0.07* (0.046**)	0.44 (0.27)	0.71 (0.61)	0.12 (0.19)	0.10 (0.09*)	0.71 (0.50)
Target D/E	0.74 (1.0)	0.55 (1.0)	0.89 (1.0)	0.61 (1.0)	0.77 (1.0)	0.02** (0.02**)	0.74 (0.73)	0.27 (0.26)	0.03** (0.03**)	0.39 (0.33)	0.37 (0.36)
FRN LIST	0.44 (1.0)	0.66 (1.0)	0.46 (0.0)	0.30 (0.0)	0.38 (0.0)	0.22 (0.22)	0.04** (0.05*)	0.17 (0.17)	0.25 (0.25)	0.65 (0.64)	0.63 (0.62)
Panel B:											
Inflshr	3.41 (4)	3.5 (4)	3.61 (4)	3.25 (3)	3.07 (3)	0.63 (0.58)	0.39 (0.43)	0.19 (0.21)	0.08* (0.08)*	0.02** (0.03)**	0.56 (0.55)
Inflbond	1.39 (1)	1.5 (1)	1.32 (1)	1.55 (1.5)	1.29 (1)	0.63 (0.42)	0.91 (0.89)	0.65 (0.65)	0.47 (0.68)	0.93 (0.94)	0.54 (0.55)
Inflemp	1.27 (1)	1.18 (1)	1.34 (1)	1.1 (1)	1.36 (1)	0.67 (0.66)	0.86 (0.62)	0.72 (0.80)	0.46 (0.29)	0.97 (0.92)	0.58 (0.45)
Inflgovt	1.11 (1)	1.17 (1)	1.27 (1)	0.70 (0.50)	1.21 (1)	0.82 (0.79)	0.25 (0.53)	0.93 (0.69)	0.09 (0.16)	0.89 (0.99)	0.13 (0.18)
Infllogovt	0.73 (0)	0.75 (0.5)	0.82 (0)	0.65 (0)	0.64 (0)	0.87 (0.87)	0.78 (0.71)	0.76 (0.80)	0.60 (0.84)	0.63 (0.88)	0.98 (0.91)
multiple	0.36 (0)	0.18 (0)	0.27 (0)	0.44 (0)	0.64 (1)	0.58 (0.6)	0.18 (0.17)	0.03** (0.03)**	0.27 (0.27)	0.04** (0.04)**	0.33 (0.32)
issuestk	0.77 (1)	0.42 (0)	0.66 (1)	0.75 (1)	0.69 (1)	0.14 (0.14)	0.06* (0.06)*	0.18 (0.17)	0.48 (0.47)	0.82 (0.82)	0.73 (0.72)
freefloat	0.67 (0.62)	0.89 (0.99)	0.63 (0.50)	0.61 (0.55)	0.70 (0.74)	0.15 (0.0)***	0.001*** (0.002)***	0.025** (0.03)**	0.88 (0.33)	0.66 (0.07)*	0.27 (0.25)
eqcost	0.105 (0.096)	10.0 (10.0)	9.8 (9.5)	9.5 (9.0)	14.0 (13.0)	0.76 (0.64)	0.39 (0.32)	0.02** (0.04)**	0.67 (0.50)	0.004*** (0.02)**	0.003*** (0.012)**
CAPM	0.77 (1)	0.81 (1)	0.83 (1)	0.83 (1)	0.4 (0)	0.91 (0.91)	0.92 (0.92)	0.05* (0.05)*	1.0 (1.0)	0.007*** (0.009)***	0.017** (0.021)**

Table XVII
Industrial characteristics of respondents across legal systems

The Contingency table analysis is used to test the dependence between the industry and legal systems among respondent firms. The value of the test statistic (Chi-Square with 21 degrees of freedom) is 18.38 and p-value is 0.63 which fails to reject the null hypothesis of independence between industry and legal systems.

Legal System	No. of Respondent Firms	Industry								Total
		Retail and wholesale	Mining and construction	Manufacturing	Transport and energy	Communication and media	Bank, finance and Insurance	High technologies (software, etc.)	Other	
English Law Countries	12	0.0%	16.7%	8.3%	8.3%	16.7%	8.3%	25.0%	16.7%	100.0%
French Law Countries	40	10.0%	22.5%	10.0%	7.5%	10.0%	22.5%	7.5%	10.0%	100.0%
German Law Countries	21	0.0%	14.3%	14.3%	9.5%	0.0%	19.0%	28.6%	14.3%	100.0%
Scandinavian Law Countries	14	14.3%	0.0%	21.4%	7.1%	7.1%	14.3%	28.6%	7.1%	100.0%
Total	87	6.9%	16.1%	12.6%	8.0%	8.0%	18.4%	18.4%	11.5%	100.0%

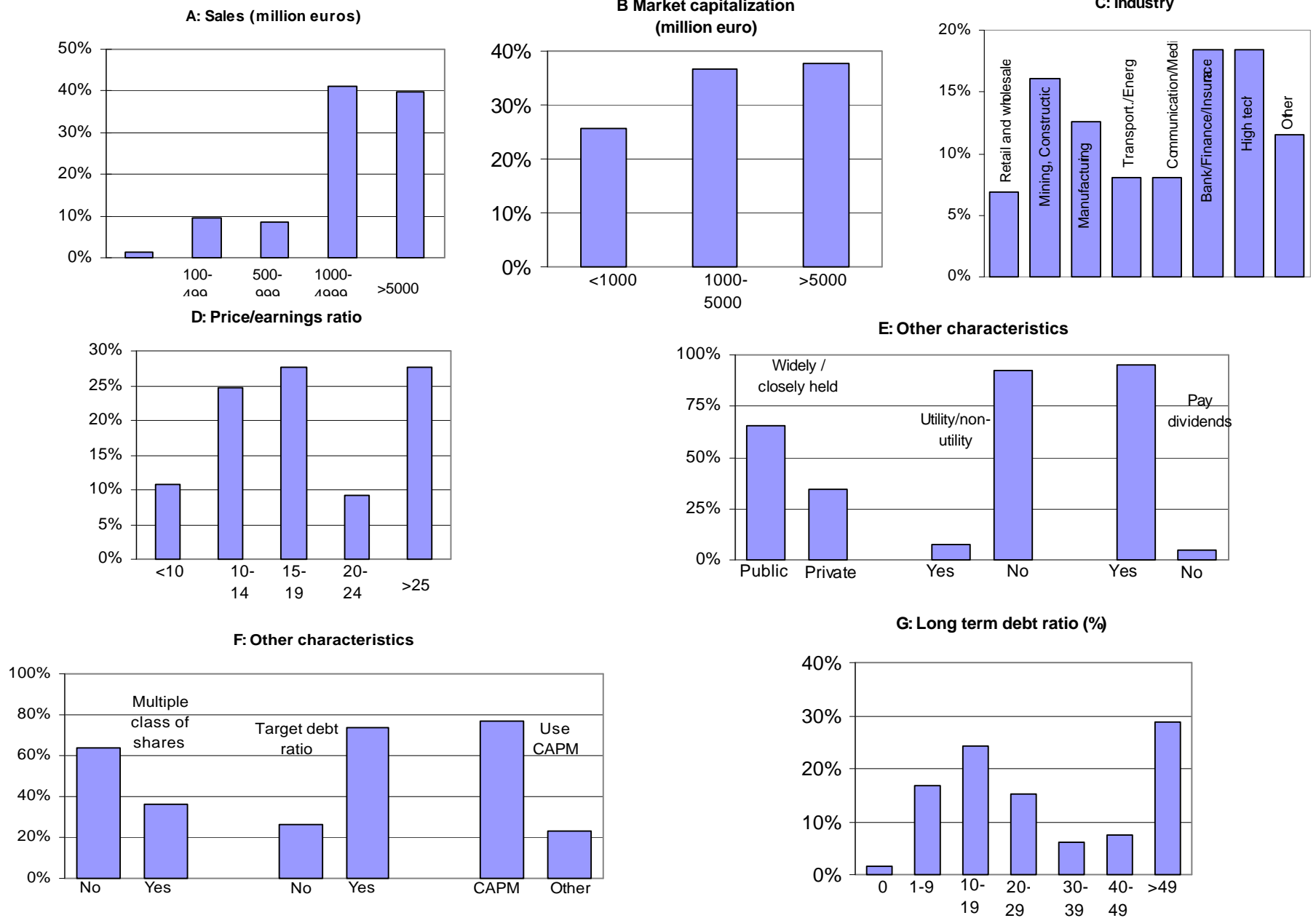
Table XVIII

Tests of Non-Response Bias across legal systems: Firm Characteristics

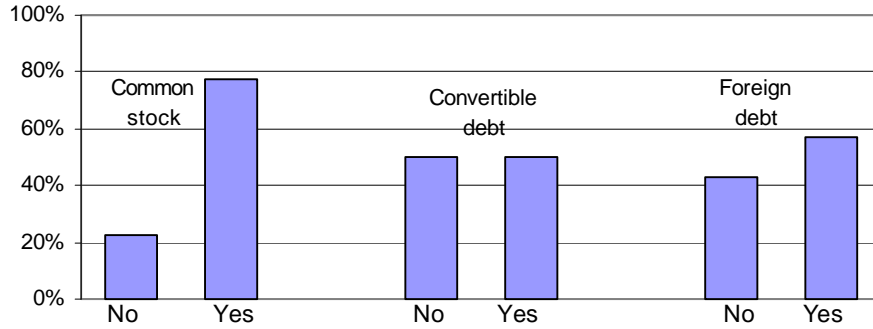
P-value for Market Cap and P/E ratio is the probability for t- test of differences in means and for Wilcoxon test of differences in medians (in parentheses). P-value for Dividend paying firms is the probability for the Fisher test that proportions of dividend paying firms is same in population and respondents across each legal system. The value (0.13) in the last row and column is the p-value of the multinomial (Chi-square) test that the proportions of dividend paying firms across all legal systems among the population are the same as among the respondents namely 85.62%, 87.80%, 76.53%, and 86.61% across French, German, Scandinavian and English law countries.

Legal System of the Country of Origin	Number of firms with data	Market Capitalization			P/E			Dividend		
		Population	Respondents	P-value	Population	Respondents	P-value	Population	Respondents	P-value
		Market Cap Average (Median)	Market Cap Average (Median)	(Wilcoxon test)	P/E Ratio Average (Median)	P/E Ratio Average (Median)	(Wilcoxon test)	Percentage of Firms pay divd	Percentage of Firms pay divd	
French Law Countries	320	7786.23 (2421)	10373.8 (2730)	0.31 (0.37)	31.25 (21.006)	19.27 (15.4)	0.15 (0.072)	85.62%	92.11%	0.33
German Law Countries	136	9842.4 (2264.4)	8553.77 (1800)	0.78 (0.66)	23.59 (19.5)	18.35 (17.5)	0.28 (0.57)	87.80%	100.0%	0.13
Scandinavian Law Countries	104	4442 (932.9)	11214.5 (1300)	0.17 (0.12)	30.06 (15.8)	17.86 (12.5)	0.27 (0.43)	76.53%	100.0%	0.07*
English Law Countries	147	14422.91 (5180.6)	18301.84 (5375)	0.68 (0.95)	31.19 (17.26)	22.5 (17)	0.56 (0.99)	86.61%	88.89%	1.00
Total	707	9009.5 (2657.6)	11245.6 (2910.5)	0.34 (0.32)	29.46 (19.3)	19.45 (16.0)	0.05* (0.07*)	84.85%	91.36%	0.13

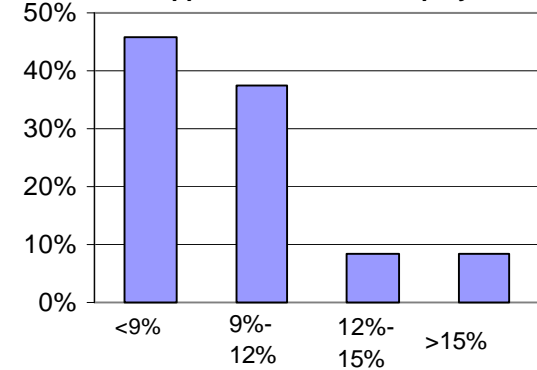
Figure 1



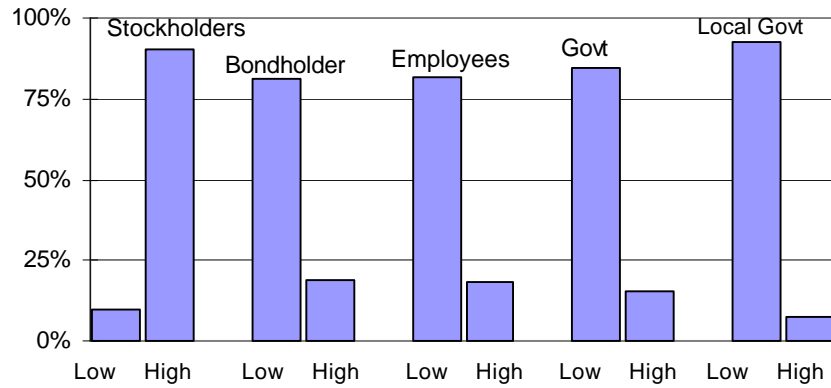
H: Percent that seriously considered issuing...



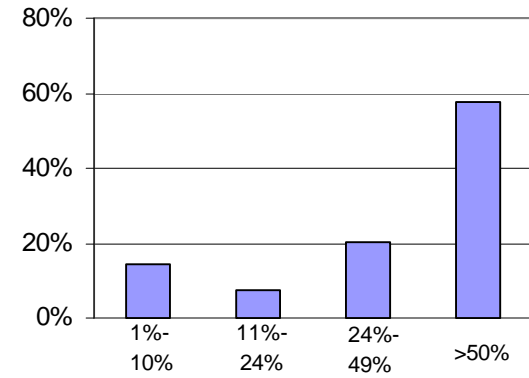
I: Approximate cost of equity



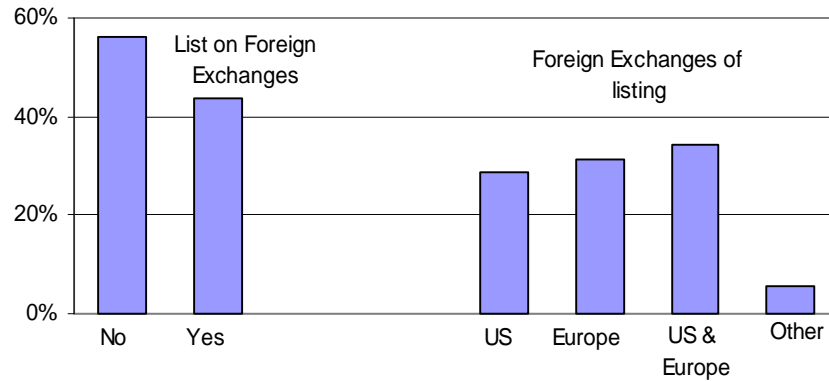
J: Influence of Stakeholders on Financing decisions



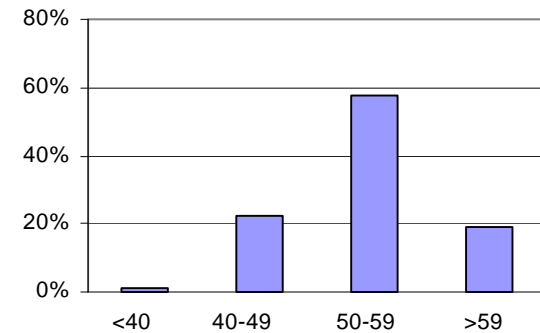
K: Foreign Sales (% of total)



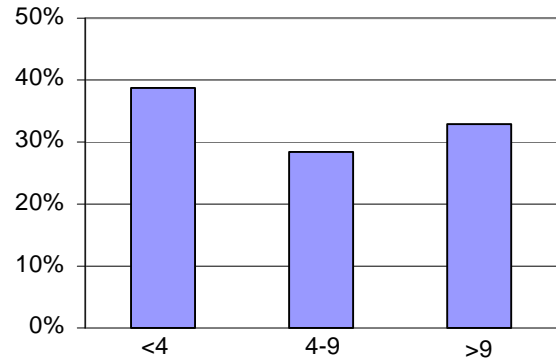
L: Foreign Listing



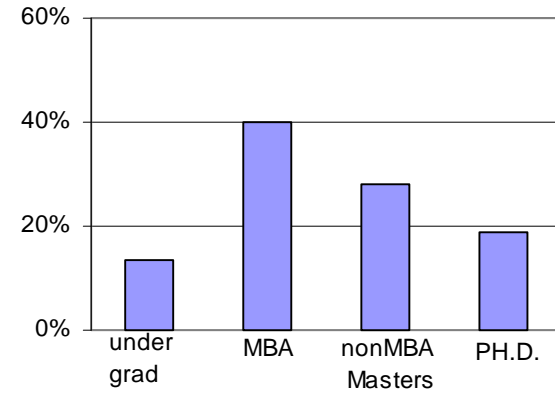
M: CEO Age (Years)



N: CEO Tenure (Years)



O: CEO Education



P: Exec. stock ownership

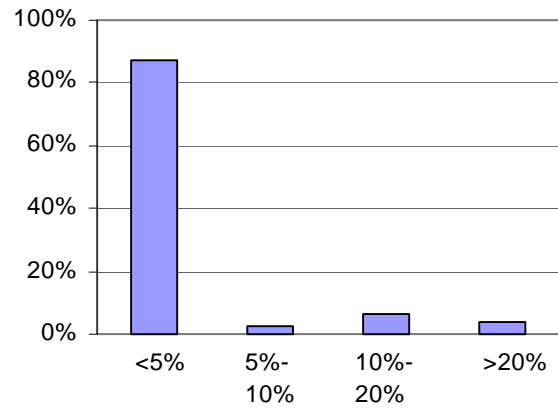


FIGURE 2: HOW TO CHOOSE THE AMOUNT OF DEBT

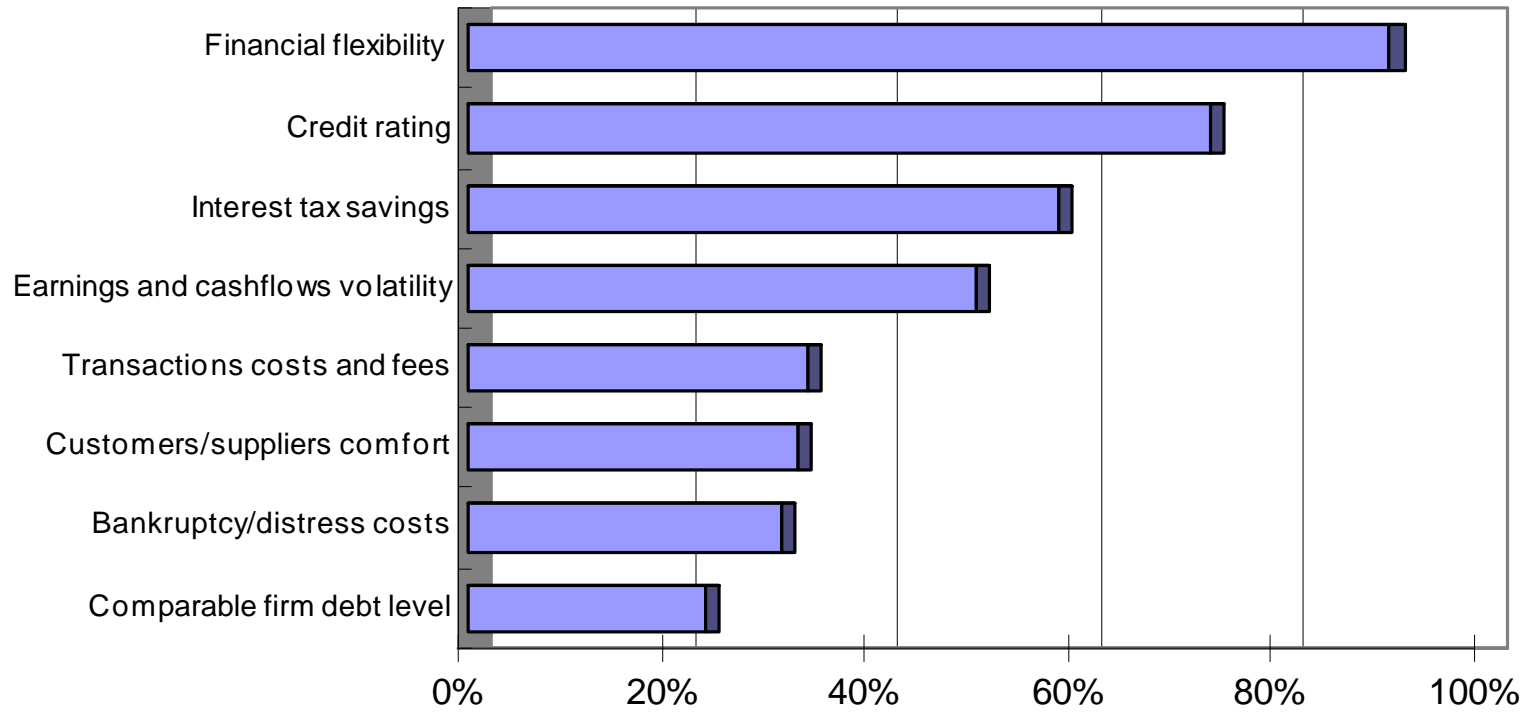


FIGURE 3: SELECTING THE MATURITY OF DEBT

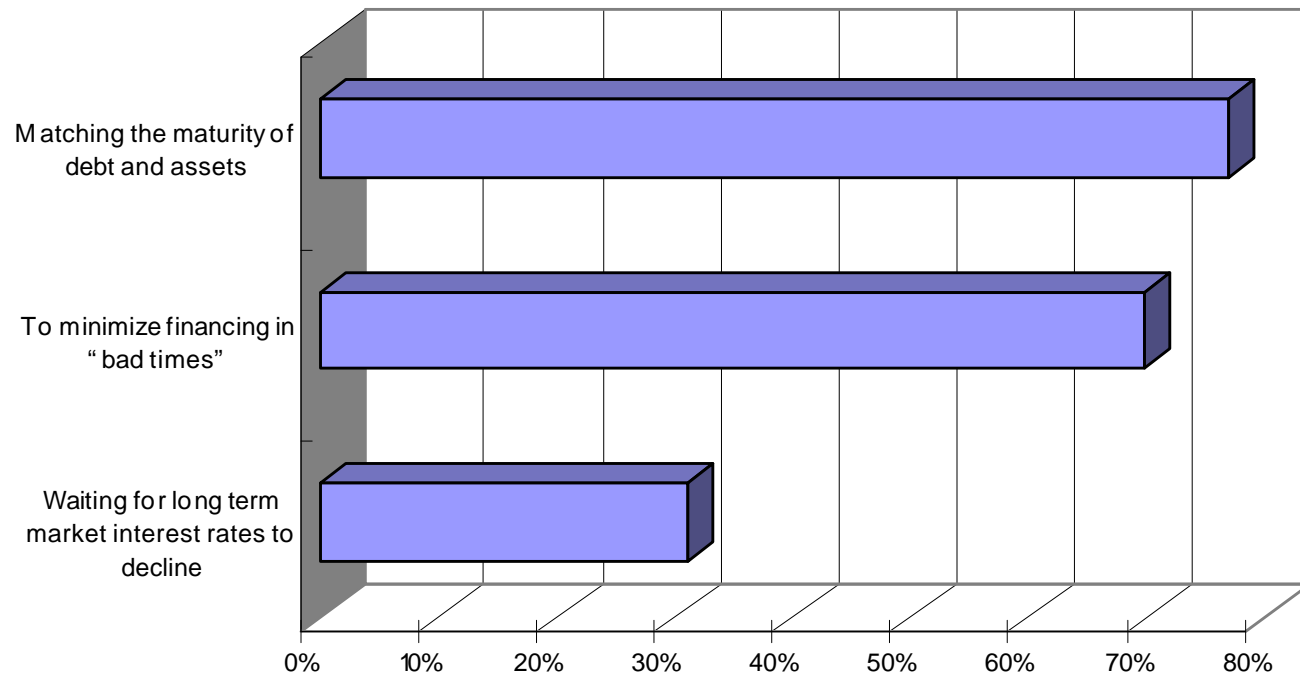


FIGURE 4: COMMON STOCK POLICY

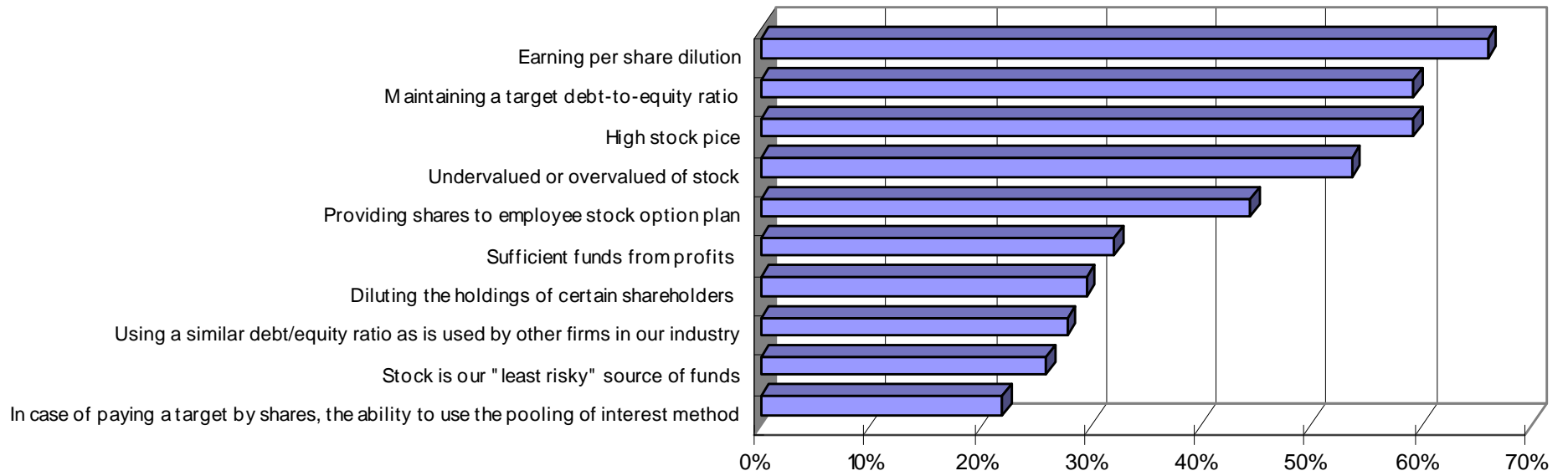


FIGURE 5: CONVERTIBLE POLICY

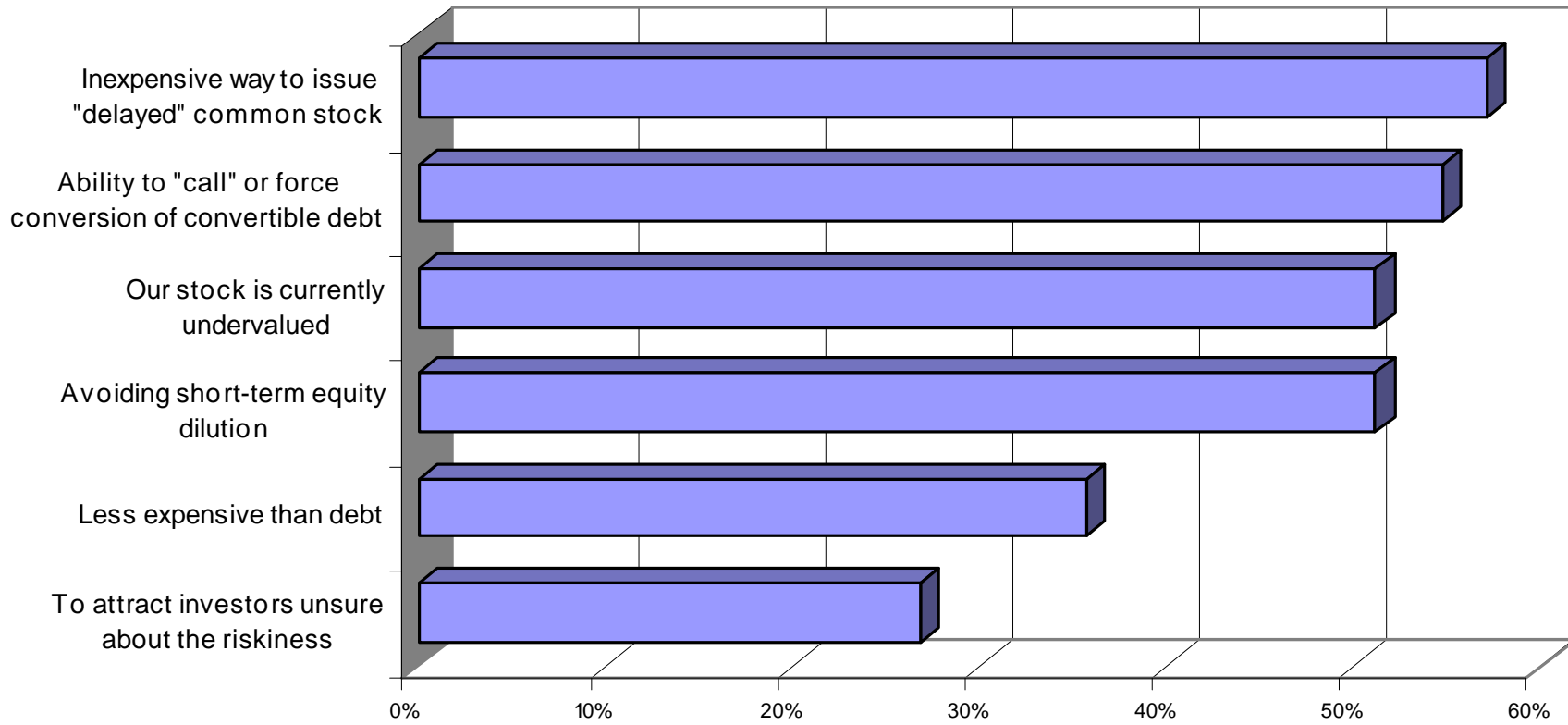


FIGURE 6: FOREIGN DEBT POLICY

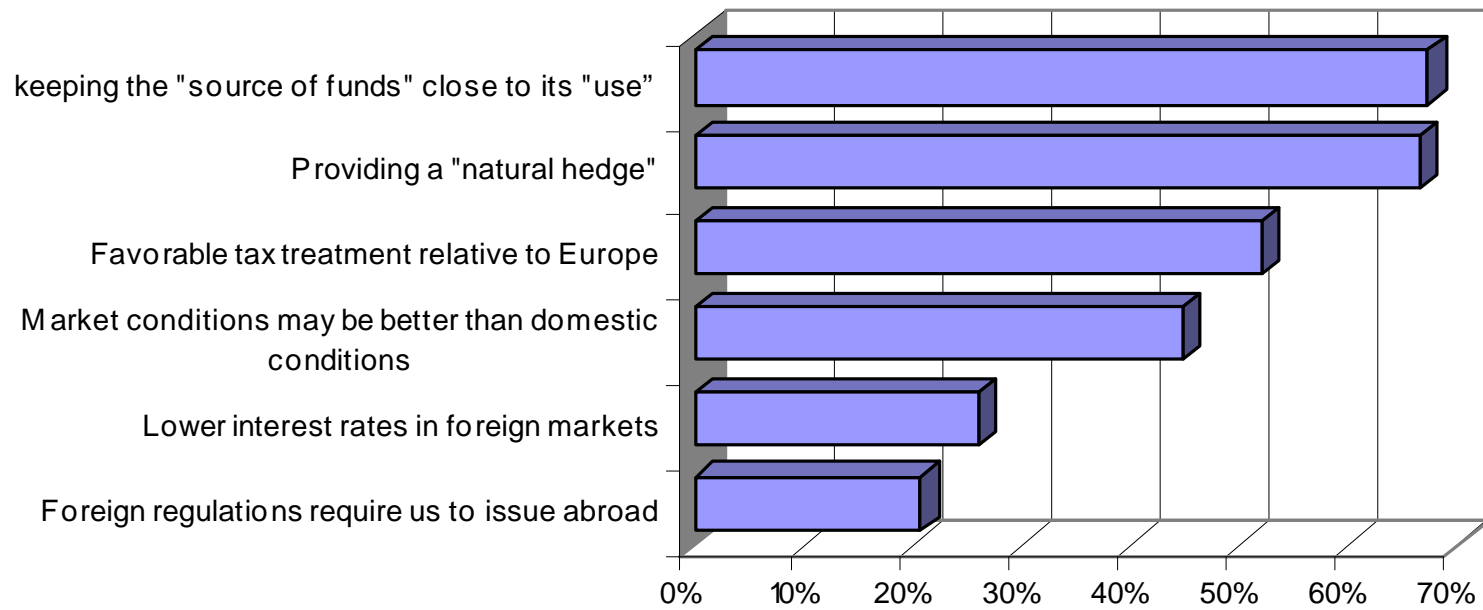


FIGURE 7: MANAGERIAL RESPONSES ACROSS DIFFERENT LEGAL SYSTEM COUNTRIES - DEBT POLICY

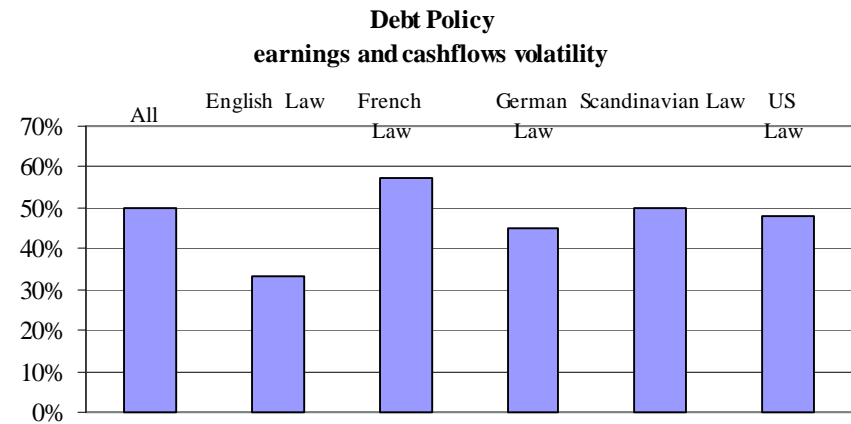
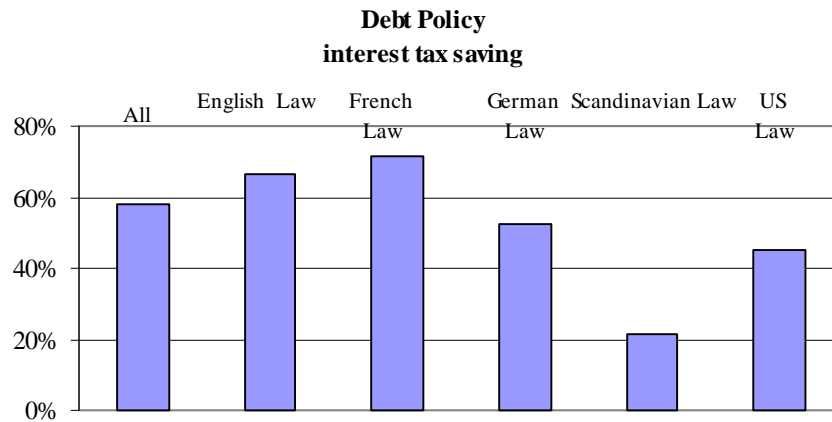
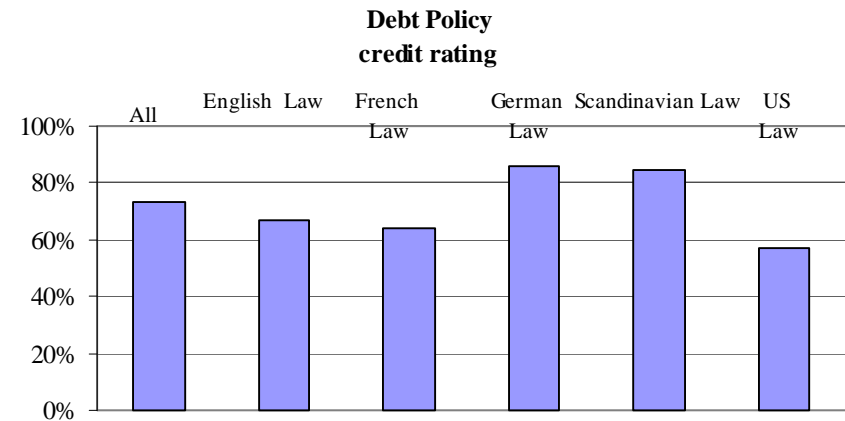
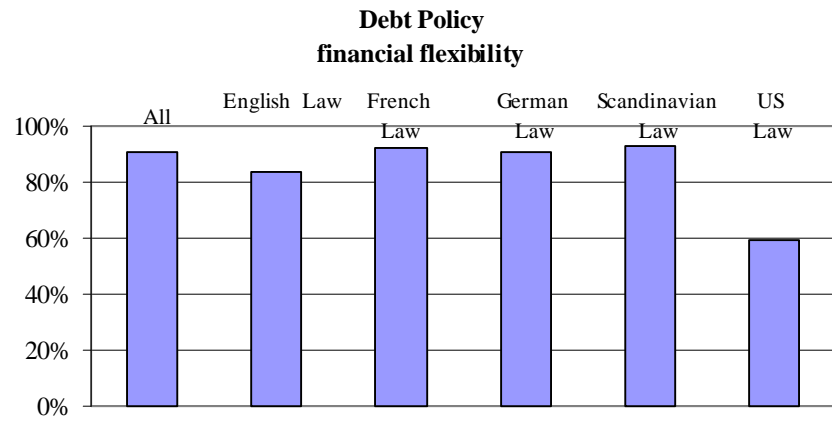


FIGURE 8: MANAGERIAL RESPONSES ACROSS DIFFERENT LEGAL SYSTEM COUNTRIES - DEBT MATURITY POLICY

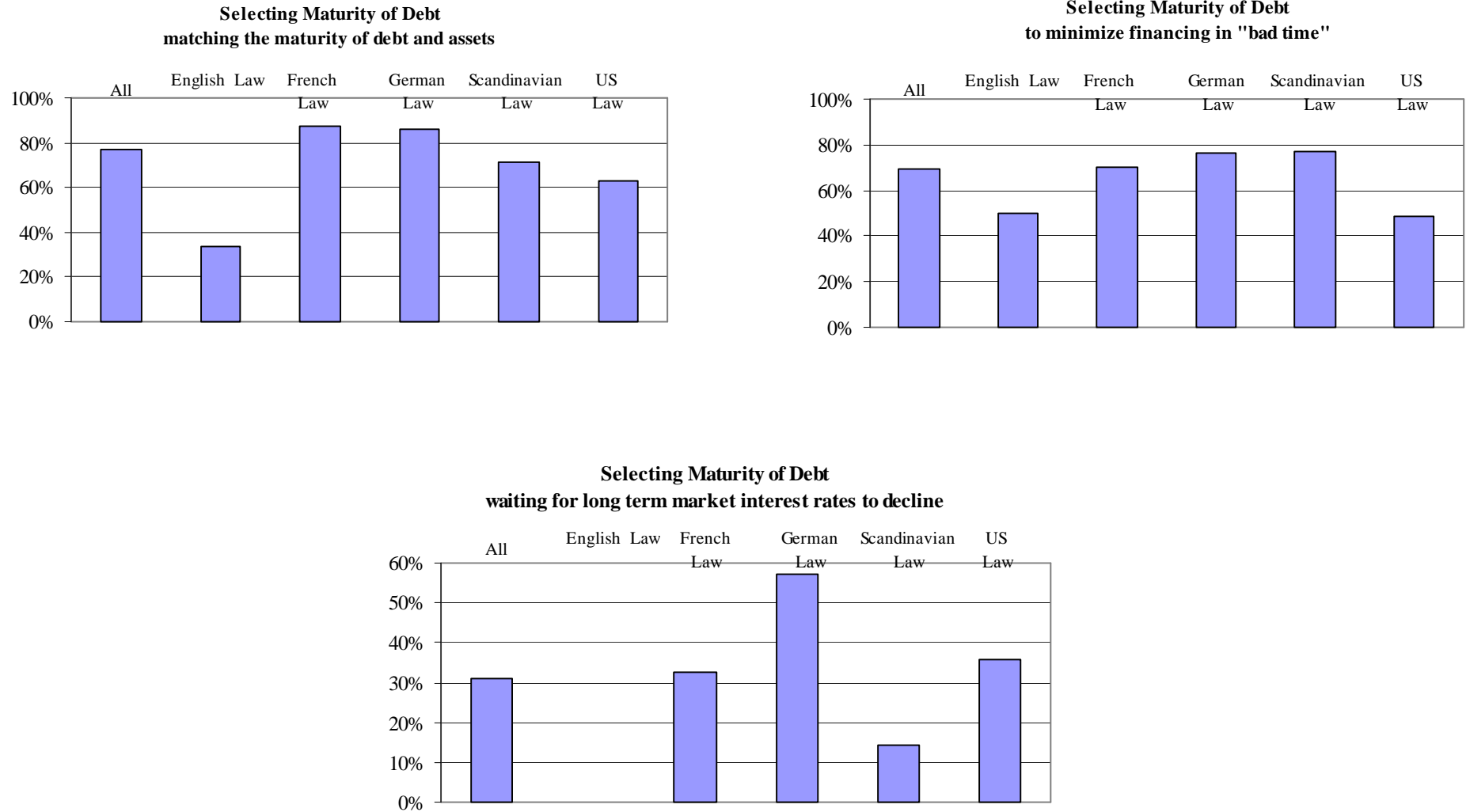


FIGURE 9: MANAGERIAL RESPONSES ACROSS DIFFERENT LEGAL SYSTEM COUNTRIES – COMMON STOCK POLICY

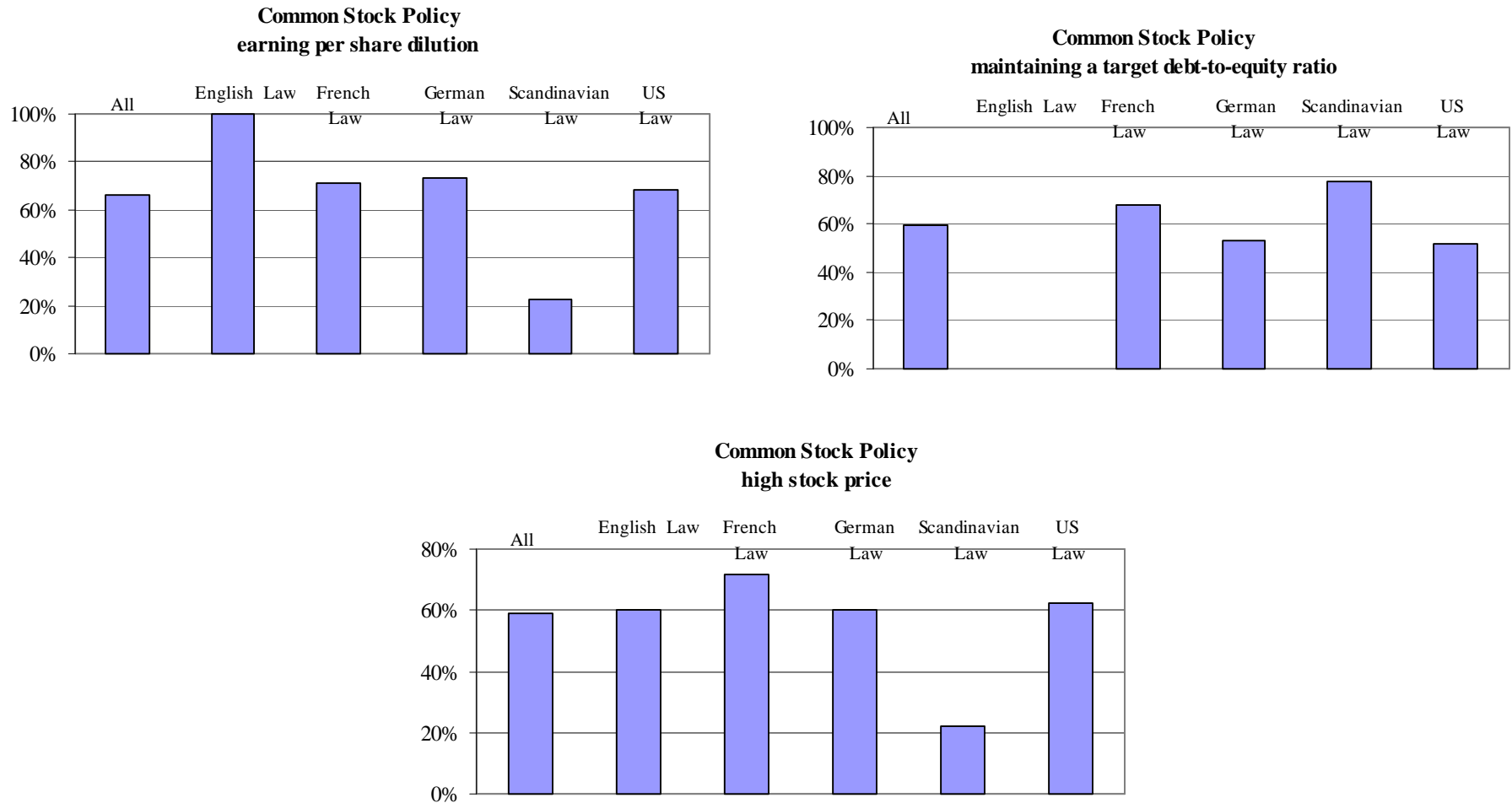


FIGURE 10: MANAGERIAL RESPONSES ACROSS DIFFERENT LEGAL SYSTEM COUNTRIES – CONVERTIBLE DEBT POLICY

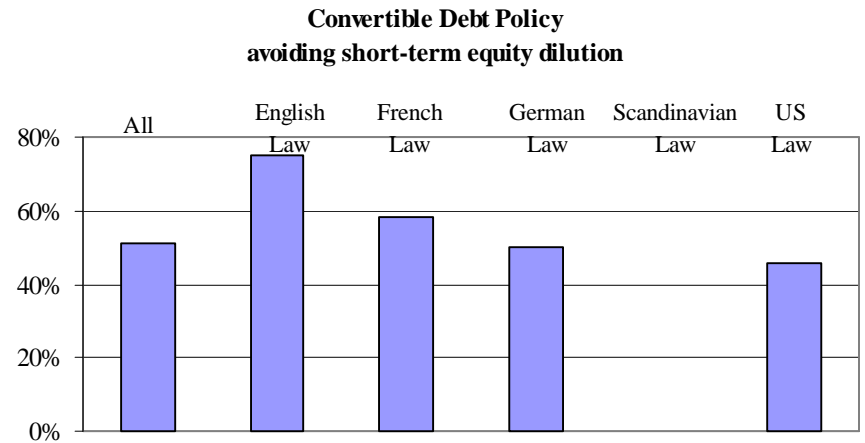
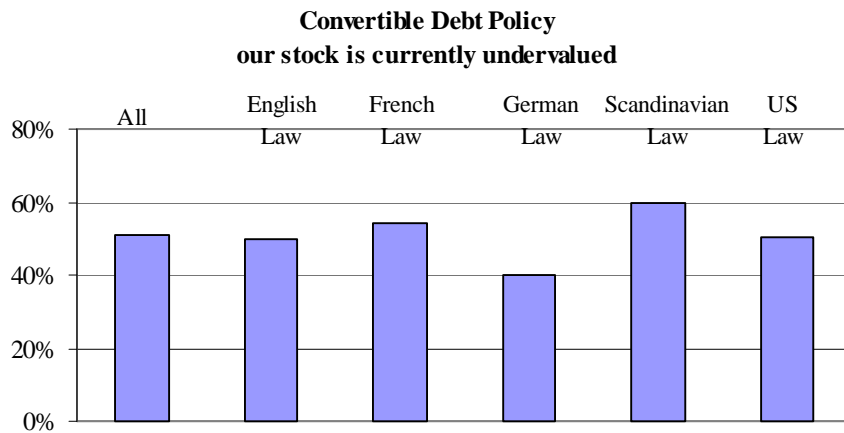
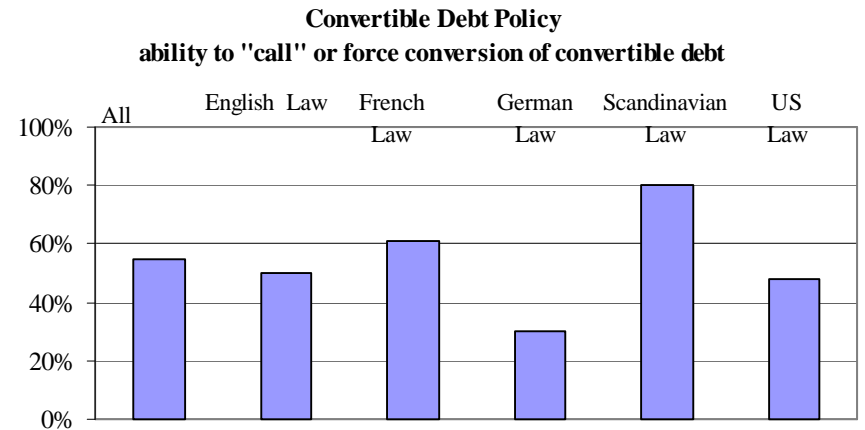
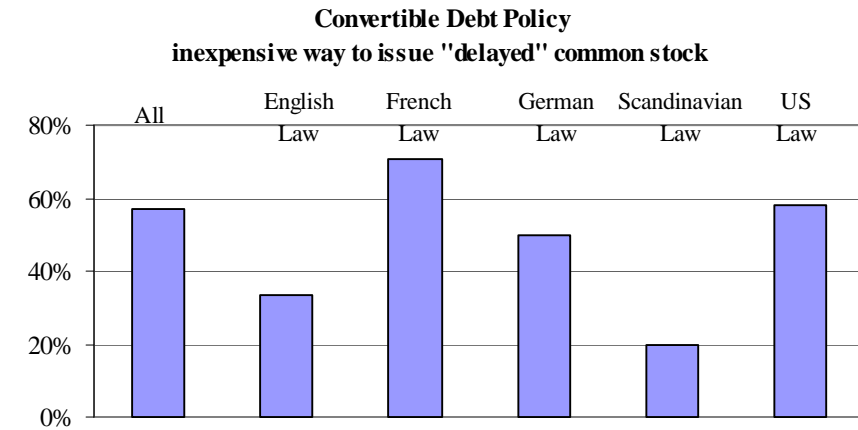


FIGURE 11: MANAGERIAL RESPONSES ACROSS DIFFERENT LEGAL SYSTEM COUNTRIES – FOREIGN DEBT POLICY

