

A Closer Look at Dividend Omissions: Payout Policy, Investment and Financial Flexibility*

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ABSTRACT

We adopt a comprehensive approach to studying dividend omissions to better understand the motivation behind this important policy decision. We find that poor operating performance, poor financial flexibility, high investment and increased risk are factors that affect the likelihood of a dividend omission. Not all dividend omissions, however, are the same. For 25 % of dividend omitting firms, the omission signals a quick turnaround in their operating performance and results in a resumption of dividends within three years from the omission. Our analysis suggests these firms use the dividend omission strategically to improve their financial flexibility, allowing them to pursue valuable investment opportunities. The remaining firms continue to be financially constrained and under-perform their peers after the omission. One possible explanation for this divergence in performance is the quality of their management.

A negative stock price reaction to dividend reduction announcements is a stylized fact (Dielman and Openheimer, 1984; Healy and Palepu, 1988). DeAngelo, De Angelo and Skinner (1992) show that dividend reductions usually occur after a period of poor operating performance and that these actions “reflect the low level of current and expected future earnings” of the firm. However, this does not imply that the firm should continue to consistently under-perform after the dividend change. Although dividend reducing firms still realize losses in the immediate periods following the reduction in dividends, studies have documented a material improvement in earnings shortly thereafter.¹

A survey of chief financial officers (CFOs) conducted by Brav, Graham, Harvey and Michaely (2005) reveals that firm payout policy remains very conservative: managers seek to maintain the existing level of dividends and avoid having to cut dividends except in extreme circumstances. This is driven, in part, by the negative market reaction to dividend reductions. Daniel, Denis and Naveen (2007) provide evidence supporting this view: S&P 1500 firms respond to cash shortfalls by reducing investments as opposed to reducing dividends. Also consistent with this view, De Angelo and De Angelo (1990) show that financially distressed NYSE firms are quite reluctant to omit a dividend. Both these studies find stronger effects if the firm has been paying dividends for a long time. Thus, we have come to expect that a dividend omission must be a “last resort” effort to get a firm out of financial distress.

In this paper we take a closer look at dividend omissions. Our objective is to better understand the motivations for omitting a dividend. To achieve this, we investigate whether the omission was actually beneficial to the firm. Specifically, we investigate

¹Bernatzi, Michaely and Thaler (1997), Grullon, Michaely and Swaminathan (2002), and Lie (2005).

whether dividend omissions are instrumental to a firm's recovery and if yes, to what extent. To the best of our knowledge, these issues remain largely unanswered in the literature. We shed light on these important topics and add to our understanding of payout policy in general. Our findings also have broader implications for firm financial policy and underscore the importance of financial flexibility in investment and financing decisions. The evidence suggests financial flexibility is of first order importance to better-managed firms.

Using a sample of 434 well-established dividend paying firms in the U.S. that omitted their regular dividend between 1963 and 2004, we find the following: First, firms that omit a dividend have low profitability and poor financial flexibility (high debt overhang or excess leverage). These firms out-spent their industry peers, in terms of capital expenditures, at a time when their risk (market risk and idiosyncratic risk) was higher overall.

Second, we find that not all dividend omissions are the same. For twenty-five percent of dividend omitting firms in our sample, the dividend omission signaled a quick turnaround in operating performance that eventually resulted in a resumption in dividend payment within three years from the omission. These firms, which we call *resumers*, eliminated their debt overhang which gave them the financial flexibility to pursue valuable investment opportunities. *Non-resumers*, meanwhile, had persistent debt overhang, low investment and continued to under perform their industry peers.

Third, compared to non-resumers, we find resumers omit their dividend when they have less compelling reasons to do so, namely: 1) they have higher sales growth and lower leverage in the year of omission; 2) investor sentiment is against omitting a

dividend in the year they omit²; 3) their poor performance is likely due to a temporary cash flow shock (as opposed to something more persistent); and 4) they could potentially still cut their dividend instead of omitting. Moreover, these firms resume regular dividend payment as soon as their profitability improves -- which occurs within three years from the omission. These findings suggest that the omission was a strategic decision that paid off for resumers. We posit that resumers have managers who recognize the urgency of the omission in order to turn the firm around. We provide some evidence that suggests these managers are “high quality” managers.

We focus on dividend omissions, instead of dividend reductions, for three reasons: First, the firm life cycle theory of dividends predicts that significant changes in dividend policy reflect significant changes in the firm’s life cycle. Just as a dividend initiation is an important policy change within the context of a firm’s life cycle (Bulan, Subramanian and Tanlu, 2007), so too is a dividend omission. Second, Baker and Wurgler (2004) show there is time-varying preference for dividend-paying stocks relative to non-dividend paying stocks. A dividend omission changes the category of a firm from a dividend-payer to a non-dividend payer, which would clearly affect investor perception of the firm a drastic way. Finally, DeAngelo and DeAngelo (1990) show firms display a stronger reluctance to dividend omissions versus dividend cuts, which suggests that the omission is generally perceived as the “last resort.”

The remainder of the paper is organized as follows: In Section I, we motivate our study from the perspective of the firm life cycle theory of dividends. Section II explains

² Investor sentiment for dividend paying stocks is measured by Baker and Wurgler’s (2004) dividend premium, i.e. the log difference in market-to-book ratios of dividend payers and non-payers. We find that firms are “punished” with a more negative abnormal stock return at the announcement of omission when the dividend premium is higher.

the data and variable construction. In Section III, we investigate the factors that lead to a dividend omission. In Section IV, we show that not all dividend omissions are the same. In Section V, we argue that some firms use the dividend omission strategically to achieve a quick turnaround in their performance. Section VI concludes.

I. Dividend Omissions in a Firm's Life Cycle

For this study, it is useful to think of dividend omissions within the framework of the firm's life cycle. Recent empirical evidence has been strongly supportive of the firm life cycle theory of dividends.³ The theory is based on the idea that as a firm matures, its ability to generate cash overtakes its ability to find profitable investment opportunities. Eventually, it becomes optimal for the firm to distribute its free cash flow to shareholders in the form of dividends.⁴ Thus, changes in firm payout policy reflect life cycle changes within the firm. For example, Bulan, Subramanian and Tanlu (2007) show firms that initiate dividends are mature firms – although, the timing of dividend initiation does not signal precisely the event of firm maturation but occurs after the transition to maturity.⁵ Along similar lines, a dividend omission would be the optimal policy response if a mature firm was to transition into a “new growth” phase, e.g. a firm reinvents itself by entering new markets with valuable growth opportunities. In this new growth phase,

³Fama and French (2001), Grullon, Michaely and Swaminathan (2002), DeAngelo, DeAngelo and Stulz (2006), Denis and Osobov (2008), Megginson and von Eije (2008).

⁴ Mueller (1972) first proposed this idea in the more general context of the agency problem within the firm. The theory is presented using a simple model in Bulan and Subramanian (2008). DeAngelo and DeAngelo (2006) present a more general “trade-off” theory of payout policy that incorporates the firm life cycle theory of dividends.

⁵ The timing of the initiation is driven by market sentiment. On the other hand, Grullon, Michaely and Swaminathan (2002) show that dividend changes (increases/decreases) signal changes in firm risk that is consistent with firm maturity, i.e. young, fast-growing firms are more risky while older, mature firms are less risky.

returns on investment exceed the firm's cost of capital and it is optimal to retain cash flows instead of paying them out.

In reality, this policy response is less likely to occur due to the strong preference of managers to maintain their payout levels, i.e. once a dividend-payer, always a dividend payer. Moreover, DeAngelo and DeAngelo (2007) argue that a good dividend payment history allows firms greater access to external equity markets – a benefit that counteracts the cost of cash flow retention (e.g. agency costs). Instead, dividend omissions are often the result of poor operating performance and financial distress, whereby the omission is part of an effort to conserve cash. Under the life cycle hypothesis, if the firm recovers from this period of poor performance and returns to a more “normal” phase of maturity in its life cycle, then we would expect it to eventually resume paying dividends. If the firm somehow recovers and transitions into a new growth phase, we might not expect the firm to resume dividend payment altogether. Another possibility is the eventual decline of the firm in which case it is acquired by another firm or its assets are liquidated.

We motivate our empirical tests within this life cycle framework. Our basic strategy is to look at a firm's life cycle characteristics over the seven year period around a dividend omission. These characteristics include operating performance, investment, growth opportunities, financing measures and risk. Just as a dividend initiation is indicative of firm maturity, we can test whether a dividend omission indicates a significant change in the firm's life cycle such as transition to a new growth phase or firm decline.

This empirical approach implicitly incorporates other theories of payout policy as well, since the life cycle theory is not exclusive of other theories. For example, agency

costs due to cash flow retention vary with the firm's life cycle (Jensen, 1986; DeAngelo and DeAngelo, 2006; DeAngelo, DeAngelo and Stulz, 2006). These costs are lower in the young, high growth phase and increase as the firm matures. Thus, payout in a firm's mature phase is consistent with agency theories. Signaling theories can be incorporated by examining the (unexpected) change in profitability and other firm characteristics around a dividend omission. Other theories such as catering (Baker and Wurgler, 2004) and tax clienteles (Allen, Bernardo and Welch, 2000) are easily nested within the life cycle framework.

II. Data and Variables

A. Sample

Our data comes from the CRSP and Compustat databases for the period 1963-2004. Following previous work on dividends, we limit the sample to non-financial and non-utility firms paying regular dividends, i.e. any distribution recorded in the CRSP database that has share codes equal to 10 or 11, distribution codes equal to 12XY and 4-digit SIC codes not equal to 49YY or 6YYY, where X is equal to 3, 4 or 5 and Y stands for any digit. Using CRSP data on dividend payment history, a potential dividend omission is identified when a firm has not paid a dividend within 1 quarter, 6 months or 1 year from the previous payment if the firm pays quarterly, semi-annual or annual dividends respectively. In this identification, we allow for "late" payments and define a 3-year period to consist of 1128 days or approximately 31 days in a month.

From this pool of potential dividend omissions, we identify actual omissions and *omission announcement dates* from the *Wall Street Journal Index* and *Lexis-Nexis*. An

observation is labeled an omission when either the *Wall Street Journal Index* or a news article found on *Lexis-Nexis* states that the firm will suspend payment of its regular cash dividend. We keep firms that have at least a 10-year history of regular dividend payments prior to the omission to ensure our sample consists of firms with a good dividend payment record.⁶ This results in a final sample of 434 omissions. In table I we provide a breakdown of the number of omissions each year. From this sample, 16 firms (3.6 %) were eventually delisted from their exchange within three years from the omission announcement⁷.

B. Variables

In our analysis, we require Compustat data for the seven years centered on the omission year. The main variables that we construct from Compustat are the following: firm size (log of total assets), profitability (ROA or return on assets), sales growth, capital expenditures scaled by total assets, market-to-book ratio (as a proxy for growth opportunities), cash holdings scaled by total assets, and book leverage. We calculate industry-adjusted measures of these variables by subtracting the two-digit SIC industry median value of the variable each year. Details of these calculations are described in the appendix. We impose standard outlier rules at the 1 % tails of the data.

We also calculate annual risk measures using a firm's daily returns⁸ from CRSP and estimate the three factor model of Fama and French (1993):

$$r_{it} - r_{ft} = \alpha_i + \beta_M (r_{Mt} - r_{ft}) + \beta_{SMB} r_{SMBt} + \beta_{HML} r_{HMLt} + \varepsilon_{it} \quad (1)$$

⁶ This is similar to Healy and Palepu (1988) and Michaely, Thaler and Womack (1995).

⁷ Of these, 5 firms were involved in a merger, 2 were delisted in an exchange of stock, 3 firms were declared insolvent and the rest were delisted for not meeting exchange requirements.

⁸ We use daily returns for the entire fiscal year with at least 50 days of non-missing return data.

where r_{it} is the firm's daily return at time t , r_f is the corresponding risk free rate, r_M is the daily return on the market portfolio, r_{SMB} is the small-minus-big (SMB) factor and r_{HML} is the high-minus low (HML) factor. Data on the factors is obtained from the Fama-French factors database on WRDS. The factor loadings are the market beta, SMB beta and HML beta respectively. The SMB beta captures small firm risk. The HML beta inversely captures growth firm risk, i.e. a higher (lower) HML beta indicates risk characteristics resembling value (growth) stocks. The standard deviation of residuals (annualized) is the measure for idiosyncratic risk. Table II provides descriptive statistics of our sample firms in the omission year.

Next, we calculate the cumulative abnormal returns on a stock in the three-days around an omission announcement as follows:

$$AR_{it+k} = r_{it+k} - r_{ft+k} - b_M(r_{Mt+k} - r_{ft+k}) + b_{SMB}r_{SMBt+k} + b_{HML}r_{HMLt+k} \quad (2)$$

$$CAR_i = \sum_{k=-1}^{+1} AR_{it+k} \quad (3)$$

In equation 2, t is the omission announcement date and AR_{it+k} is the abnormal return on stock i on the k th trading day relative to the announcement date. b_M , b_{SMB} and b_{HML} are the Fama-French three-factor betas. CAR_i is the cumulative abnormal return in the 3-day window around the announcement.

Alternatively, we calculate cumulative excess returns (CER) in the 3-day window around the omission announcement date according to Michaely, Thaler, Womack (1995):

$$CER_i = \prod_{-1}^{+1} (1 + r_{it}) - \prod_{-1}^{+1} (1 + r_{Mt}). \quad (4)$$

In equation 4, $t=0$ is the omission announcement date, r_{it} is the daily return on stock i on day t , and r_M is the daily return on the CRSP value weighted index. In the same manner, we construct holding period excess returns (or market adjusted returns) for each of the three years following the omission as follows:

$$\text{Excess Return}_{ik} = \prod_2^k (1 + r_{it}) - \prod_2^k (1 + r_{Mt}) \quad (5)$$

where k is the number of trading days one, two or three years after the omission announcement date. This is the buy and hold return on the stock where the strategy is to buy the stock one day after the omission announcement.⁹

In Table III we present the CARs and CERs for our omission sample. As expected, the mean (and median) 3-day cumulative abnormal return around the dividend omission announcement is negative. Moreover, 80% of these dividend omissions have negative cumulative abnormal returns around the announcement date. Figure 1 shows the holding period returns for each of the three years after the omission. The median firm's market-adjusted holding period return is consistently negative in the three years omission. Michaely, Thaler, and Womack (1995) document this phenomenon as drift, i.e. prices continue to drift in the same direction as predicted by the CAR for at least one year after the omission.

III. Why do firms omit a dividend?

In this section, we identify the factors that affect the likelihood of dividend omissions. We find poor operating performance, high investment, financial *inflexibility* and high risk are determinants of a dividend omission. Firms that omit their dividend are

⁹ r_{it} is the one day return from $t-1$ to t , hence the index starts at $t=2$.

going through a “tough time.” These mature firms, who are well-established dividend payers, experience operating and financial difficulties which eventually result in a dividend omission. Given the negative announcement effects of dividend omissions, our findings are ambiguous in support of signaling theories. What is unambiguous, however, is the high leverage ratios of these firms leading into the omission that persists thereafter. This financial inflexibility is an important result that we explore further in the paper.

A. Firm Characteristics Around the Omission

We first document the characteristics (industry-adjusted) of dividend omitters in the seven years centered on the omission year in Figure 2. These patterns are consistent with prior work. There is a sharp decline in ROA and sales growth in the three years leading into the omission year, where they achieve their lowest levels below the industry median. ROA and sales growth improve gradually after the omission. The market-to-book ratio displays the same U-shaped pattern. However, these three measures don't fully return to their pre-omission levels by the third year after omission. Capital expenditures on the other hand is high initially, declines sharply leading into the omission, then recovers slightly thereafter -- indicating that firms are scaling back their investments. On the financing side, we find that leverage increases sharply in the years leading into the omission and remains at this high level thereafter while cash holdings declines towards the omission and recovers thereafter. In terms of risk, there is an overall increasing trend in all the risk measures over the seven years centered on the omission year.

In sum, we find dividend omitting firms suffered declining operating performance which likely resulted in severe financial constraints as indicated by increasing leverage

and declining cash levels. The severity of these conditions not only resulted in a reduction in capital spending but also led to the dividend omission. After the omission, firms replenish their cash holdings but continue to have very high, above-industry leverage. Furthermore, they have become riskier. Operating performance improves gradually in the three years after the omission, but is still short of its pre-omission levels.

B. Matched Sample Logit Analysis

Next, we conduct matched-sample logit analyses to identify which firm characteristics are significant in explaining the decision to omit a dividend. In the previous section we have controlled for industry performance, while in this section, we further control for dividend-paying status. We construct a matched-sample of dividend omitting firms and non-omitting control firms according to industry (two-digit SIC), size (assets) and profitability (ROA). We identify control firms from a pool of dividend-paying firms from CRSP with at least a ten year history of regular dividend payments – the same requirement we impose on our sample of omitting firms. For each dividend omitting firm from our sample, we choose a control firm from the same industry that is closest in size and profitability in the year prior to the omission. To implement this, we first partition industries into size quartiles. Within the size quartile of the dividend-omitting firm, we choose the non-omitter that is closest in ROA to the dividend omitter. This gives us a sample of 407 dividend omitters paired with an industry-size-profitability matched firm that paid a dividend in the year of the dividend omission. Thus, each pair

of firms faces the same general market conditions in the years surrounding the omission.¹⁰

We then estimate logit regressions to identify factors affecting the omission decision (Table IV). The dependent variable equals 1 if the firm is a dividend omitter. The independent variables are measured prior to the omission year to ensure that they are pre-determined. In column 1 we measure firm characteristics in the year prior to the omission year (lagged), while in column 2 we measure these variables as an average of the three years prior to omission (lagged 3-year average). In the table we report marginal effects, dP/dx , where P is the predicted probability of being a dividend omitter and x is an explanatory variable. All marginal effects are evaluated at the mean values of the variables. We report p-values calculated from bootstrapped standard errors adjusted for correlation within industries.

The results of these regressions confirm prior work but also reveal fresh insights. Firms that omit a dividend have low profitability and high leverage. What is revealing is these firms have been spending more on capital expenditures in the three years prior to the omission despite no significant difference in their growth opportunities (market-to-book ratios) compared to the non-omitters. This higher spending also occurred at a time when their risk was higher overall, i.e. high market risk and high idiosyncratic risk. These findings indicate poor performance and high investments coupled with financial inflexibility (high leverage) and high risk are factors that led to the omission. From column 1, a 10 % decrease in profitability (ROA) increases the likelihood of being a

¹⁰We also implement a matching strategy where we partition each industry into ROA quartiles and choose the control firm closest in size within the omitting firm's ROA quartile: the results are similar to those we report here.

dividend omitters by 12.5 %. This would be equivalent to the effect of a 28 % increase in leverage or a 12 % increase in idiosyncratic risk, all else constant.

Next, we estimate this matched-sample logit model as a function of the (unexpected) change in firm characteristics after the omission. Under a rational expectations assumption, we measure this change as the difference between the three-year variable averages post- and pre-omission in column 3¹¹ and as the difference between the variable's three year average post-omission and its value in the omission year in column 4, while controlling past performance (lagged three-year averages of all firm characteristics). In the former, we are interested in the (unexpected) post-omission performance relative to the pre-omission years while in the latter, we are interested in the (unexpected) post-omission performance relative to the omission year itself when operating performance was at its lowest level.

Relative to the omission year, we find the profitability and cash ratios of dividend omitters improve, idiosyncratic risk declines but market risk increases. Relative to the three years preceding the omission, there is no change in the profitability of dividend omitters but there is a significant reduction in their capital spending. Both cash ratios and leverage are higher after the omission. The SMB beta and idiosyncratic risk are both higher. These results suggest the following: 1) the omission does not signal continued poor operating performance; 2) omitters have curbed their investment activities with no apparent change in their growth opportunities; 3) the omission helped these firms

¹¹These specifications can also be viewed as a test of signaling theories.

conserve cash; and 4) leverage and idiosyncratic risk, which were already higher before the omission, increased even further after the omission.¹²

Since the leverage measure we use is adjusted for the industry median leverage, it can also be interpreted as a measure of excess leverage or *debt overhang*, i.e. the difference between actual firm leverage and the firm's target leverage ratio¹³. Myers (1977) argues that a large debt overhang could cause a firm to under-invest, i.e. to forgo positive net present value projects by limiting the firm's ability to raise funds to finance them. Existing work has shown debt overhang adversely affects investment and firm value.¹⁴ We shall see later in our analysis that this is particularly relevant for a subset of dividend omitters, especially since leverage increases further after the dividend omission.

In terms of idiosyncratic risk, Hoberg and Prabhala (2005) find it is negatively related to the propensity to pay dividends. They argue that idiosyncratic risk serves as a proxy for growth opportunities or cash flow risk. Bulan, Subramanian and Tanlu (2007) find that declining idiosyncratic risk is associated with firm maturity and an increased propensity to initiate dividends. These studies suggest high idiosyncratic risk is related to the risk profile of young, high growth firms while low idiosyncratic risk is related to the risk profile of older, mature and stable firms. Within the firm life cycle framework, our

¹²Given these results, it is unclear whether dividend omitting firms are using the dividend omission as a signal of future performance. Grullon, Michaely and Swaminathan (2002) - although they look at dividend decreases and not dividend omissions - find that the negative market reaction to dividend decreases can be attributed in part, to increased systematic risk. Lie (2005) finds that the negative market reaction to omission announcements can be attributed to poor performance in the quarter of the announcement.

¹³Our results are robust to using a target leverage ratio estimated according to Kayhan and Titman (2007). This target leverage ratio is the predicted value from a regression of firm leverage on various explanatory variables known to affect capital structure.

¹⁴Lang, Ofek and Stulz (1996) show that leverage negatively affects growth for firms with low growth opportunities. Hennessy (2004) demonstrates that the underinvestment problem is more severe for long-lived assets and that debt overhang has a negative effect on investment regardless of the ability of the firm to raise fresh secured debt.

finding that dividend omitting firms have higher idiosyncratic risk indicates a deviation from the earnings stability and low-risk profile of mature firms.

C. Reason for the Omission

Given the results thus far, we find the combination of high capital expenditures and low profitability resulted in financially constrained firms that eventually omitted their regular dividend. It is informative to look at the reason(s) for the dividend omission provided by the firm at the time of the announcement. We present a summary of these in Table V. Surprisingly, 66 % of firms did not provide any specific cause or explanation for the dividend omission. Twenty-five percent attributed the necessity of the omission to poor performance such as earnings losses and in many cases, these firms also cite poor market conditions. A small fraction (9 %) of the group attempted to put the omission in a more positive light by highlighting strategic motives either to fund existing or future investments or to preserve financial flexibility. As we shall see throughout the paper, this theme of investment and financial flexibility resonates in our analyses. More importantly, this type of reasoning by firms suggests that the dividend omission was not just a reaction to past (dismal) performance, but also a strategic response to improve future performance. It is this issue of strategic omissions that we turn to next.

IV. Is the Omission Beneficial to the Firm?

It is well-established that managers are extremely reluctant to omit a dividend. On the other hand, our findings above suggest that a dividend omission might be an optimal policy response for a firm experiencing financial difficulties. We can thus

conjecture two kinds of dividend omissions: one where the omission was simply the last resort effort to get the firm out of its financial difficulties, or one where the omission was more of a strategic decision that was the right thing to do at the right time.¹⁵ In this section, our empirical strategy consists of identifying a group of dividend omitters for which the omission not only indicates a turnaround in firm performance, but also results in superior firm performance after the omission. We then look back to the time of the omission and investigate the factors that motivated the omission as well as the factors that may have led to superior post-omission performance. Our goal is to identify firms which benefitted from the dividend omission

A. Resumers and Non-Resumers

We have seen that on average, dividend omitting firms show an improvement in operating performance in the three years following an omission. However, a better indicator of the size and permanence of these improvements might be the actual resumption behavior of these firms. If these omitting firms believe that their performance has “turned the corner” in that their gains are concrete enough and sustainable, then they may resume paying regular dividends soon after, consistent with the life cycle theory. On the other hand, if a firm does not resume dividend payments despite an improvement in performance, this could be because it is not confident of being able to sustain the good

¹⁵ DeAngelo and DeAngelo (1990) find that dividend reductions may be driven, in part, by strategic reasons such as to improve a firm’s bargaining power with labor unions.

performance¹⁶ or it could indicate that the firm has transitioned to a different life cycle phase, i.e. firm decline.

In table VI, we present the fraction of omitters that resume paying dividends in each of the three years following the omission. Given that these firms were undergoing operating and financial difficulties, it is surprising to see a steady number of firms resume dividend payments soon after the omission. Nearly 25 % of our sample resume dividend payments within three years from the omission. This fraction is surprisingly high, considering that over 80% of omissions produce a negative stock price reaction. Although in total 51 % of the firms resume paying dividends within our sample period, we limit the resumption window to 3 years after omission for two reasons: first, we are interested in instances where the omission is used to help turn the firm around from its financial difficulties; and second, we expect this turnaround to occur within a reasonable period of time from the omission.

In order to confirm that these resumptions are indeed the result of superior performance, in Figure 3 we present industry-adjusted operating performance measures of the resuming and non-resuming firms in the seven years centered on the omission year. We perform both t-tests and ranksum tests of the equality of means and medians for all these performance measures¹⁷. We find no significant difference in profitability and sales growth between resumers and non-resumers in the three years prior to omission with the exception of sales growth in year -2. In the post-omission period, resumers outperform the non-resumers. As early as the omission year, resumers are already more profitable

¹⁶Along similar lines, DeAngelo, DeAngelo and Skinner (1992) use a sample of NYSE firms that experienced earnings losses during 1980-1985 and show firms that reduced their dividends experienced more severe and more persistent losses compared to those that did not reduce their dividends.

¹⁷ While figure 3 shows the results for means, the results for medians are similar and the differences are even more significant in most cases.

and have higher sales growth than non-resumers and this difference is significant.

Moreover, resumers have bounced back to industry levels by the second year after omission.

There is no significant difference in growth opportunities (market-to-book ratios) between the two groups over this seven-year period with the exception in year -2 where resumers have lower market-to-book ratios. We have already seen that capital expenditures are declining over this period. What is surprising is that capital expenditures for resumers are consistently above that of non-resumers, and these differences are significant in years -3, -2, +2 and +3. Meanwhile, cash holdings declines towards the omission year and improves thereafter, with resumers having significantly more cash after the omission. Leverage ratios increase towards the omission. A stark difference between the two groups is their leverage post omission. Non-resumers' leverage ratios remain significantly high above industry-levels after the omission (positive debt overhang), while resumers are able to maintain lower leverage ratios that are similar to their industry peers (zero debt overhang). In terms of risk, we find that resumers have significantly higher HML beta before the omission (i.e. their risk characteristics more closely resemble value stocks) and lower idiosyncratic risk from the omission year onwards.

We synthesize and interpret these results as follows: At the beginning of this period, these firms are performing well within their respective industries (if not better than the median firm). They have good financial flexibility (no debt overhang and high cash ratios) and are aggressively investing in fixed assets (above industry capital expenditures). Then, they experience a decline in sales growth and profitability (a

negative cash flow shock). They are forced to scale back their investments and increase their leverage ratios as their cash balances decline. Eventually, they are led to omit their regular dividend. What differentiates the resumers from the non-resumers is their ability to bounce back rather quickly in terms of profitability and sales growth. This enables them to replenish their cash holdings and keep leverage ratios at industry levels (i.e. their debt overhang is zero). In fact, it is only in the year of omission that resumers have positive debt overhang. Soon after, they resume their regular dividend payments and capital expenditures increase to more moderate industry levels. On the other hand, although the profitability of non-resumers improves after the omission, it improves at a much slower pace. Their cash holdings increase but leverage remains very high. This high debt overhang constrains their investments.

B. Stock Return Performance

We have thus identified two groups of omitters, where one group outperforms the other in terms of ROA and sales growth in the three years after the omission. Do we see this difference in performance reflected in their stock returns? In Figure 4 we see that this is indeed the case. Holding period returns of resumers are significantly positive and significantly higher than for non-resumers in both means and medians. This difference is even more stark when looking at market adjusted (or excess) returns. Resumers outperform the market in the three years post-omission. Non-resumers' holding period returns are either negative or not significantly different from zero. At best, non-resumers perform as well as the market in the three years following the omission¹⁸.

¹⁸ A natural question to ask given this stark difference in post-omission stock returns is can we predict resumers at the time of the omission? This is an interesting question that is analyzed in Bulan,

C. Cumulative Abnormal Returns

We saw in Table III that nearly 20 % of omissions have a positive announcement effect. Do these correspond to the resumers? More specifically, do these positive announcement effects correspond to firms that announce the omission is strategically motivated to improve future performance? In Table VII we present the mean and median 3-day omission announcement effects (cumulative abnormal returns) of resumers and non-resumers. Two main points may be noted here: first, there is no significant difference in the announcement effects for resumers and non-resumers; second, resumers have a significantly negative announcement effect. Thus, investors treat the dividend omission of both resumers and non-resumers equally as bad news.

Investigating further, we regress the cumulative abnormal return against a dummy variable for resumers, the firm's dividend history, Baker and Wurgler's (2004) dividend premium in the year of the omission, and the reason for the omission provided by the firm at the time of the announcement. We calculate the dividend history variables in the following manner: 1) pre-omission dividend yield = last dividend prior to omission divided by the stock price ten days prior to the omission announcement date,¹⁹ 2) number of dividend cuts = the number of times the dividend was cut in the three years prior to the omission,²⁰ and 3) change in the last dividend = $(D_j - D_{j-1})/D_{j-1}$ where j is the dividend payment period immediately preceding the omission. These variables control for the

Subramanian and Tanlu (2008). In this paper, we focus on the dividend omission itself and its role in corporate payout policy.

¹⁹ We use the stock price 10 days prior to the omission announcement date to preclude any information dissemination related to the omission that may have occurred prior to the announcement itself.

²⁰ This is weighted by the frequency of dividend payment to account for differences in annual, semi-annual and quarterly frequencies.

element of surprise. Omissions are generally preceded by several dividend cuts (De Angelo and De Angelo (1990), Benartzi, Michaely, and Thaler (1997)) that signal a gradual deterioration in performance. Additionally, a larger dividend prior to the omission could generate a more negative market reaction. We include the dividend premium to examine whether dividend omissions are instances of firms catering to shifts in investor preferences (i.e. market sentiment) for dividend paying stocks. Lastly, we include dummy variables for explanations related to strategic reasons and break this down into two dummies to separately capture the need to finance current/future investments and the need for financial flexibility.

The regressions are presented in table VIII. The coefficient on the dividend yield prior to omission is negative and the coefficient on the number of dividend cuts prior to omission is positive, and both are significant. These results suggest that the element of surprise was greater (a more negative abnormal return) for firms that were paying higher dividends and for firms that had a fewer number of dividends cuts prior to the omission. The coefficient on the dummy variable for resumers is positive, but not significant. Thus, the similarity in abnormal returns between resumers and non-resumers remains even after controlling for the size of the surprise element in each case. The coefficient on the dividend premium is negative and significant, indicating that the market penalizes firms for omitting when the dividend premium is high. Moreover, if the omission of resumers in our sample were simply instances of catering to market sentiment, then they would have positive announcement effects, rather than the negative effects that we have documented. Finally, the dummy variables for omission explanations related to strategic

reasons have no effect on the market's reaction to the announcement.²¹ If any, we find that firms announcing the omission will free up cash needed to finance current/future investments have a slightly less negative abnormal return. This evidence is weak, but it points to the possible role of strategic omissions in our analysis.

D. Multivariate Logit Analysis

Next, we perform logit regressions of the type of ommitter on key firm characteristics (Table IX). The dependent variable equals one if the firm is a resumer and is zero if a non-resumer. In columns 1-6, we are interested in firm characteristics prior to the omission or contemporaneous to the omission year, while in columns 7-8, we are interested in the (unexpected) changes in these variables after the omission. The explanatory variables are measured either in the year of omission (columns 1-2), in the year before the omission year (columns 3-4), as an average of the three years preceding the omission (columns 5-6), or as the change after the omission (columns 7-8)²². We report marginal effects evaluated at variable means and p-values calculated from bootstrapped standard errors adjusted for correlation within industry groups.

In the year of omission, resumers are firms with higher sales growth, lower debt overhang and lower idiosyncratic risk. In column 1, a 10 % increase in sales growth increases the likelihood of being a resumer by 2.7 % while a 10 % decrease in leverage (or idiosyncratic risk) increases the likelihood of being a resumer by 3.6 % (4.1 %). The effect of the dividend premium is positive and significant suggesting resumers were more

²¹ We have also tried dummy variables for poor performance explanations and whether an explanation was provided or not. These had no effect on the abnormal returns.

²² Since we use the three-year average value of each variable post-omission to measure changes in firm characteristics, these specifications also require a rational expectations assumption. See the table notes for more details.

likely to omit when the dividend premium was high. Recall from table VIII that firms that omit when the premium is high are penalized by investors with a more negative abnormal return. Thus, resumers choose to omit dividend payment at a time when investors favored dividend-paying stocks and consequently, the penalty for omitting is high.

In columns 3 through 6, we look at firm characteristics prior to the omission. We find that resumers have higher capital expenditures and are closer in risk characteristics to value firms (higher HML beta). In the year prior to omission, their leverage is lower than non-resumers. Surprisingly, their three year average sales growth is lower but their profitability is similar to non-resumers²³. The year prior to omission is when leverage between the two groups begins to diverge. In addition, resumers omitted when the dividend premium was high not only in the year of omission, but also in the three years leading up to the omission. In columns 7 and 8, we find that relative to non-resumers, resumers experience a significant increase in sales growth and cash holdings and a reduction in leverage and idiosyncratic risk. These results are all in line with figure 3.

Another exercise that we perform is to include a dummy variable that equals one when the firm gives an explanation for the omission during the announcement. Given that more than half of the firms in our sample do not provide a reason for the omission is puzzling. Firms may have an incentive to explain the necessity of the omission as part of the firm's longer-term strategy in order to mitigate the negative market reaction. What we find in Table IX is surprising: firms that do not provide a reason for omission are more likely to be resumers. We find no effects when this dummy variable is broken down further to differentiate between explanations related to poor performance versus strategic reasons. It is interesting that non-resumers are more likely to attribute the omission to a

²³This could indicate the resumers are better managed firms. We return to this point in the next section.

specific cause (poor performance, poor market conditions). Of course related to this is the larger issue of whether firms choose to reveal the real reasons behind the omission (their true type) or whether they will mimic the explanations provided by other firms, or say nothing at all. Our findings on this issue open up a lot more questions than can be addressed in this paper. We do not explore this issue further, but it is an important topic for future work.

V. Why are resumers different?

We have shown that resumers omit their dividend in a year when they are relatively better off than non-resumers in terms of sales growth, financial flexibility, and idiosyncratic risk. We have also found that resumers are penalized more heavily by the market upon announcement of the dividend omission (Table VIII). Compared to non-resumers, resumers omit dividend payments at a time when there are less compelling reasons to do so – yet they omit anyway. In this section, we explore what makes resumers different from non-resumers. What are resumers doing differently? Do resumers have the better managers? Or are these firms just luckier?

A. Cash Saved, Investment and Financial Flexibility

To address these questions, a natural starting point is to look at what firms do with the cash they save from the dividend omission. If high debt levels constrain a firm's recovery, then we should see these firms using the cash saved from the omission to reduce their debt overhang. In table X we compare the cash saved from the omission to the firm's debt overhang. Cash saved is calculated as the annualized dollar value of the cash dividend payment immediately preceding the omission, both as an absolute amount

and as a fraction of total assets. The median cash savings from the omission is not that large – about 1.6 million dollars for resumers and just under a million dollars for non-resumers. Debt overhang, however, is much larger – 3 million dollars for resumers and 5.75 million dollars for non-resumers. Thus, although the cash savings from the omission is substantial for both types of omitters, it is insufficient to completely eliminate their debt overhang.

We also checked whether firms were simply substituting stock repurchases for dividends. We define stock repurchases according to both Fama and French (2001) and Grullon, Michaely and Swaminathan (2002). We find that firms are not repurchasing shares. If any, they are actually issuing new shares in the year of omission and in the years thereafter for both groups of firms (not reported for brevity).

Given these results, two things stand out: One, the fact that non-resumers have high debt overhang that persists after the omission -- on average, non-resumers are about nine percent “over-levered” compared to their industry peers. And two, resumers actually do eliminate their debt overhang and they keep it at negligible levels in the three years following the omission. It is our interpretation that resumers are using the dividend omission, in part, to improve their financial flexibility. Not only are these firms maintaining leverage ratios at industry levels, but they are also conserving cash as evidenced by significantly higher cash holdings relative to their industry peers. Table X shows that financial flexibility appears to be a key driver of the difference in the investment policies of resumers and non-resumers. In the three years following the omission, resumers have significantly higher capital expenditures than non-resumers *and* their investment has also bounced back to industry levels. Non-resumers’ capital

expenditures remain below industry levels. Additionally, during this period there is no significant difference in growth opportunities between these firms. This further suggests that the different investment policies pursued by resumers and non-resumers is driven by their financial flexibility (or the lack thereof).²⁴ Consistent with this result, Daniel, Denis and Naveen (2007) find dividend-paying firms with greater financial flexibility reduce their investment spending less often when faced with a cash shortfall.

In sum, we find resumers eliminate their debt overhang after the dividend omission. This reduction in leverage creates much needed financial flexibility that enables these firms to pursue valuable investment opportunities. Further boosted by improving profitability, resumers eventually resume regular dividend payments. Non-resumers have high levels of debt overhang that persist after the omission. This persistence of debt overhang limits their investment and they continue to perform poorly after the omission.

B. Is it management quality?

It thus appears that the two types of dividend-omitting firms can be differentiated further into those that make good decisions and those that do not. Is management quality what drives the different decisions made by these firms? Are resumers better managed firms? Despite the strong negative reaction to dividend omissions, perhaps better managers recognize the urgency of taking the “bitter medicine,” i.e. omitting dividends, in order to heal their firm of its operating and financial malaise. Thus, these firms are using the omission strategically in order to improve firm performance.

²⁴ These patterns in investment, growth opportunities and financial flexibility are also seen annually in Figure 3.

We posit that the quality of management may be a key factor that differentiates resumers from non-resumers. Chemmanur, Paeglis and Simonyan (2007) show firms with higher quality managers are associated with higher capital expenditures and lower leverage – consistent with the characteristics of resumers that we find²⁵. Due to data limitations, we are unable to obtain detailed management characteristics for our sample. Instead, we look at top management turnover surrounding the omission. The timing of the turnover is important here. On the one hand, if the turnover occurs just prior to the omission, then a new manager might use a dividend omission to signal that he or she is intent and committed to solving the firm’s problems. On the other hand, if the turnover occurs right after the omission, this could indicate that the omission was the last straw for unhappy shareholders, resulting in the manager’s termination. In this case, our hypothesis is good managers will be retained while bad managers will be replaced.

To examine this issue, we identified the top three executives (CEO, President and Chairman) from the *Moody’s Industrial Manuals* for all the firms in our sample. We do this for four years beginning with two years prior to the omission and ending in the year after the omission (years -2 to +1). We create a *management turnover* dummy variable that equals 1 if any one of the top executives of the omitting firm was replaced in year -1 or year +1 and include it in the logit regressions. In Table XI we find that turnover prior to the omission is insignificant. On the other hand, management turnover *after* the omission is significant and it reduces the likelihood of being a resumer by about 10 % -- an economically significant result.

²⁵ They measure management quality based on the management team structure (e.g. uniformity in tenure), resources (e.g. education and experience) and reputation (e.g. number of board memberships).

Thus, resumers are more likely to retain their managers despite the dividend omission while non-resumers are more likely to replace their manager(s) after the dividend omission. Of course, we understand that management turnover is not the best proxy for management quality. At the very least, this dummy variable captures the unexpected change in management under a rational expectations assumption. We do not claim that this is overwhelming evidence to support our hypothesis. We can claim, however, that the managerial decisions made by resumers resulted in a superior outcome -- suggesting these managers made the right decisions at the right time and their continued employment in the firm supports this.

A related point is whether low quality managers are entrenched. If this were the case, it should weaken our results since the superior performing firms are the ones less likely to replace their managers after the omission. Additionally, Knyazeva (2007) finds weakly governed managers are under greater pressure from shareholders to maintain their level of dividends. If we think that resumers are better governed firms, this finding suggests resumers would be less hesitant to omit their dividend for the right reasons – further supporting our hypothesis.²⁶

C. Or is it just plain luck?

An alternative explanation for the difference between resumers and non-resumers is simply good fortune. Recall that profit levels and sales growth display a U-shaped pattern for all omitters with their lowest levels in the year of omission (or the year before in terms of sales growth for resumers). We can interpret this as evidence of a negative

²⁶ In a related paper, John and Knyazeva (2008) find that dividend policy and corporate governance are essentially “substitutes” in mitigating the agency cost of free cash flow.

cash flow shock to the firm that eventually resulted in the omission. It is possible that resumers were just luckier in that their negative cash flow shock was only temporary while that of non-resumers was more persistent. If a negative cash flow shock is temporary, then the firm is able to recover fairly quickly. On the other hand, if a negative cash flow shock is more persistent, then the firm remains in a state of poor performance for a longer period of time.

The patterns we observe in Figure 3 are consistent with this hypothesis. Non-resumers are worse off in both the level and the severity of the decline in profitability and sales growth leading into the omission year. Resumers' operating performance bounced back to industry levels within two years after the omission. Non-resumers continue to underperform their industry three years after the omission.

Luck, however, cannot be the only factor that makes resumers better off than non-resumers. Our findings show resumers should have less of an incentive to omit a dividend: 1) they have significantly better sales growth in the year of omission; 2) they have lower leverage, and hence could still potentially borrow; and 3) they face a high dividend premium. A temporary negative shock to the firm's cash flows should be another dis-incentive for omitting a dividend. If resumers have better luck and if they know that the negative cash flow shock is only temporary, then why do they still choose to omit a dividend? At the very least, prior studies suggest managers would choose to cut their dividend first (or even cut again) before resorting to an omission. To check this, we include in Table XI the number of times a firm cut its dividend in the previous three years (weighted by dividend payment frequency). We find that resumers cut their dividend less

often compared to non-resumers before deciding to omit the dividend altogether,²⁷ further supporting our claim. We also include the amount of the firm’s dividend per share prior to omission to control for very low dividends that cannot be cut further – this variable is insignificant and does not change our results (not reported for brevity).

D. Why Resume Dividend Payment Soon After an Omission?

Thus far, we find resumers are “going against the grain” when they omit their dividend. We have argued that if managers really believe the omission is necessary for a quick turnaround in their firm’s performance, then we might expect them to resume dividend payment soon after the omission. As a final exercise, we examine the dividend resumption decision of resumers using both a hazard model and a logit model. We use a hazard model to identify the factors affecting the decision to resume dividend payment from the time of the omission. We use a logit model to differentiate the resumption decision of resumers from other dividend omitting firms that resumed much later (i.e. those that resumed more than three years from omission).

We estimate the following Cox proportional hazard model²⁸:

$$\Pr(\text{Resume}_{it} = 1 \mid \text{Resume}_{ix} = 0 \quad \forall x < t) = \exp(X_{it}\beta)h_0(t). \quad (6)$$

Time t here refers not to calendar time but to time since dividend omission. All firms omit at time $t=0$. The dependent variable Resume_{it} equals 1 when firm i has resumed its regular dividend at time t ($0 < t \leq 3$); it is zero otherwise. X is a vector of time-varying firm characteristics, β is a vector of coefficients to be estimated, and h_0 is the baseline

²⁷ Also recall from Table VIII that firms with fewer number of dividends cuts prior to the omission experience a more negative abnormal return.

²⁸ We perform a test based on Grambsch and Therneau (1994) to ensure that the proportional hazard assumption is not violated in our data.

hazard function (the probability of dividend resumption as a function of time alone). Basically, we have a panel data set that tracks a firm from omission to resumption or from omission until the third year after omission, i.e. we right-censor our sample after three years.²⁹

The result of this regression is shown in column 1 of Table XII. We measure firm characteristics prior to the year of dividend resumption to ensure that they are pre-determined. The table reports hazard ratios e^{β} , where a unit change in covariate x leads to an $(e^{\beta}-1)$ percent change in the probability of resumption.³⁰ We report p-values that are calculated from bootstrapped standard errors adjusted for correlation within 2-digit SIC industry groups. Overall, we find that resumers resumed dividend payment once their profitability improved, while their debt overhang and idiosyncratic risk continue to remain low. A 10 % increase in profitability increases the likelihood of resumption within three years from omission by 42 % -- which is quite a large effect. At the same time, the dividend premium also has a significant positive effect on the propensity to resume. Thus, firms are also partly catering to investor demand for dividend paying stocks.

In column 2, we estimate a logit model where the dependent variable equals 1 when the firm is a *three-year* resumer and is zero when the firm resumes dividend payment more than three years from omission. Again, the explanatory variables are measured in the year prior to dividend resumption. We report marginal effects evaluated

²⁹ The hazard specification correctly accounts for right-censored observations. This analysis is similar to Bulan, Subramanian and Tanlu (2007) who analyze firms from IPO to dividend initiation. For the 16 firms that are delisted within three years from omission, we right-censor the data in the year prior to their last observation.

³⁰ For example, a hazard ratio of 1.05 indicates a 5 % increase in the probability of resumption while a hazard ratio of 0.95 indicates a 5 % decrease in the probability of resumption.

at the means with p-values corresponding to bootstrapped standard errors adjusted for industry correlation. This regression suggests that at the time of dividend resumption, three-year resumers are larger firms whose risk characteristics more closely resemble those of value stocks. Moreover, the profitability and sales growth of three-year resumers is lower compared to all other resumers, i.e. three-year resumers do not require a large bounce back in profits in order to resume regular dividends.

Taken together, the hazard and logit analyses suggest that one decisive factor for a dividend resumption “soon after” an omission is an immediate improvement in profitability. This early resumption displays the strong confidence managers have regarding the firm’s future performance and provides further evidence supporting our hypothesis.³¹

In sum, our findings suggest the dividend omission was more of a strategic decision for resumers as opposed to being simply a last resort response to continued poor performance. These firms were willing to accept short-term pain for long-term gain.³² Ex-post we can say that their managers made a good decision at that time -- the omission was instrumental to the quick turnaround in performance of resumers. On a related point, the evidence also suggests non-resumers perhaps waited too long to omit their dividend, bringing up the question of whether a dividend cut or a dividend omission is the optimal policy response. This is another interesting question that we leave for future work.

³¹ We also test for the impact of a firm’s institutional holdings on dividend resumptions, in order to examine the importance of tax-based dividend clienteles using data on the institutional holdings of each firm’s stock from CDA/Spectrum’s Institutional 13(f) Common Stock Holdings and Transactions database (available from 1980 onwards). We did not find any significant effects of institutional holdings on the decision to resume dividend payment.

³² In a related paper, Christie (1994) finds that the (negative) market reaction to the size of dividend reductions (including omissions) is not monotonic but instead U-shaped, i.e. large dividend cuts are penalized by the market more heavily than dividend omissions. It is possible that high quality managers realize this and hence, omit the dividend instead of having a large, but still less than a hundred percent dividend reduction.

VI. Conclusion

In this paper, we take a closer look at dividend omissions to better understand the motivations behind this important policy decision. We find that poor operating performance, poor financial flexibility, high investment and increased risk are factors that affect the likelihood of a dividend omission. Not all dividend omissions, however, are the same. For 25 % of dividend omitting firms, the omission signals a quick turnaround in their operating performance and results in a resumption of dividends within three years from the omission. Our analysis suggests these dividend resusers use the dividend omission strategically to improve their financial flexibility, allowing them to pursue valuable investment opportunities. The remaining firms continue to be financially constrained after the omission and under-perform their peers. Our findings suggest high quality managers recognize the urgency of taking the bitter medicine, i.e. the dividend omission, in order to heal their firm of its operating and financial malaise.

Our findings also highlight the importance of financial flexibility in firm policies. Recently, several studies have emphasized the role of financial flexibility in being able to reconcile theory with evidence. For example, DeAngelo and DeAngelo (2007) propose a theory of capital structure and payout policy where financial flexibility is the “critical missing link” in existing theories. Similarly, Byoun (2008) finds that accounting for financial flexibility in empirical tests helps explain perceived empirical anomalies. In this paper, and consistent with survey evidence, we show that preserving financial flexibility is of first order importance to better-managed firms.

Appendix A: Variable Definitions (CRSP-COMPUSTAT Merged Database)

Total Assets = data6

ROA = data13/data6 (where data13 = operating income before depreciation)

Sales Growth = (data12 - L.data12)/L.data12

Capital Expenditure Ratio = data128/data6

Cash Ratio = data1/data6

Book debt = data181+data10-data35-data79 (total liabilities + preferred stock - deferred taxes - convertible debt)

Book equity = data6 - book debt

Market equity = data25*data199 (shares outstanding*fiscal year end share price)

Market to Book ratio = (data6-book equity + market equity)/data6

Book Leverage = book debt/data6

R&D/Sales = data46/data12

Selling Expense/Sales = data189/data12

L is the lag operator. When data199 is missing, we replace it with the fiscal year end closing price obtained from CRSP.

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Figure 1: Post-Omission Holding Period Returns

One, two and three year holding period returns from a buy and hold strategy where the dividend omitting stock is purchased one day after the dividend omission announcement. Excess (market-adjusted) returns are calculated by subtracting the CRSP value-weighted index return over the same period.

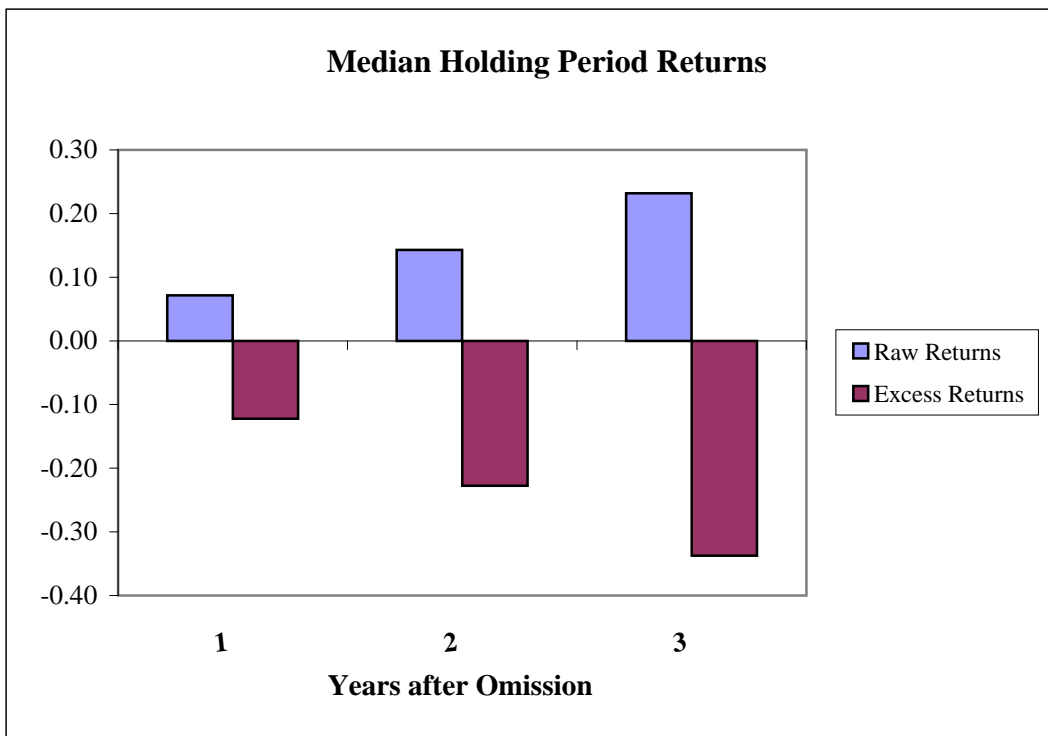
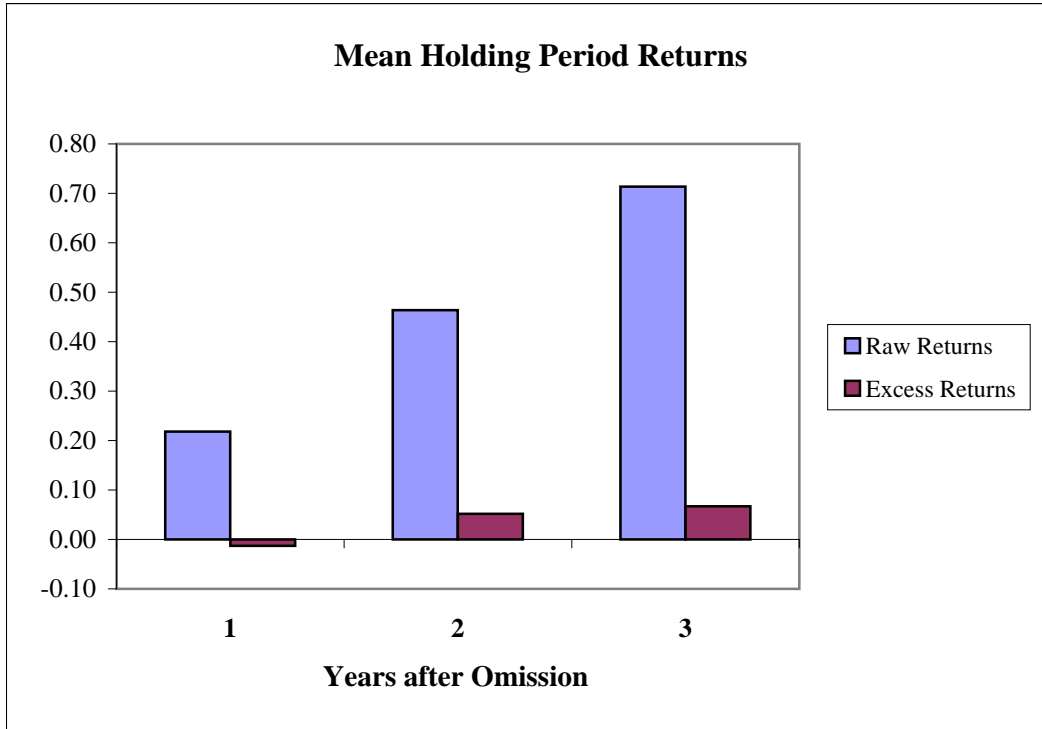


Figure 2: Firm Characteristics around the Omission

Key characteristics of dividend omitting firms in the seven years centered around the omission year. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the actual firm value. For the performance measures, capital expenditures is scaled to the right while the rest are scaled to the left. For the financial measures, leverage is scaled to the left while cash is scaled to the right.

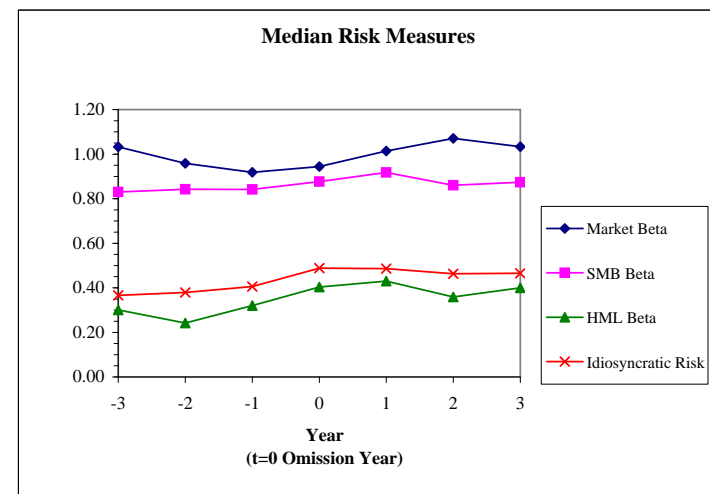
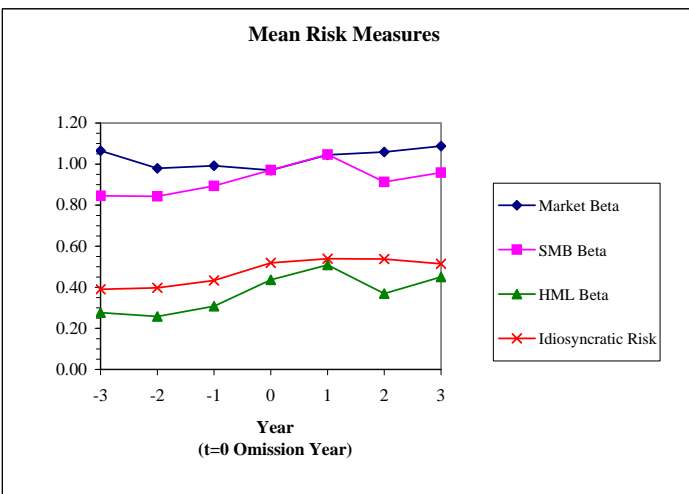
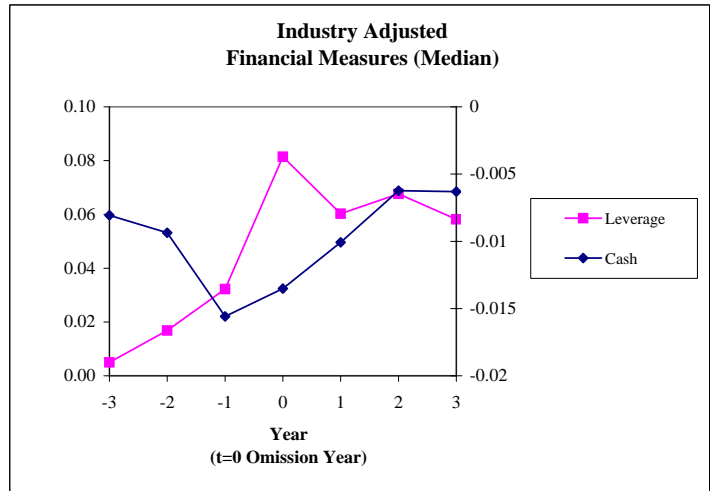
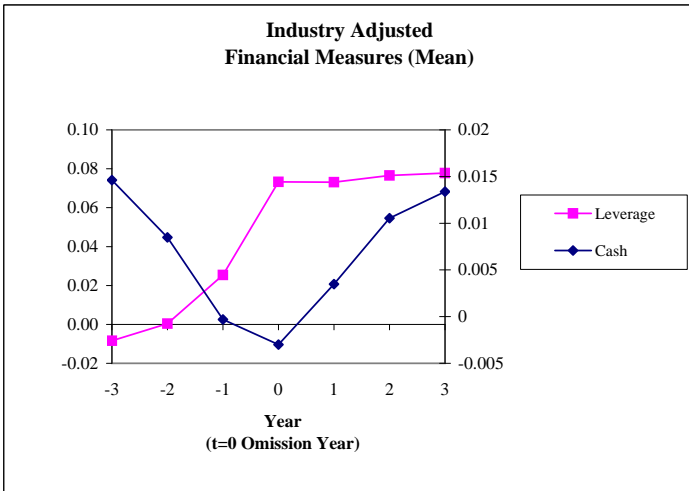
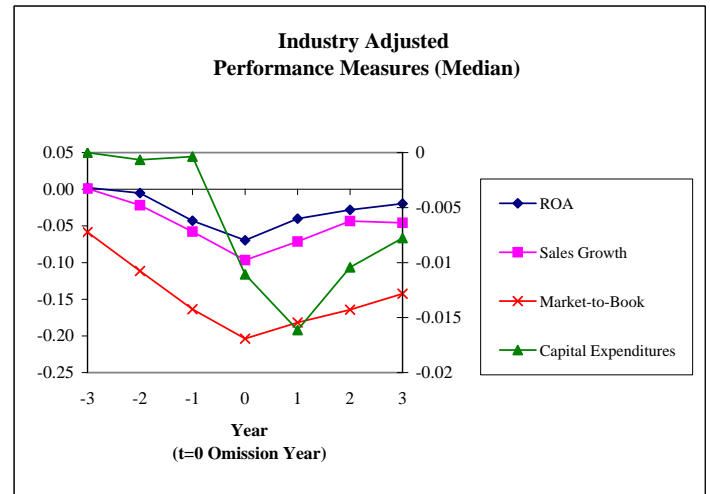
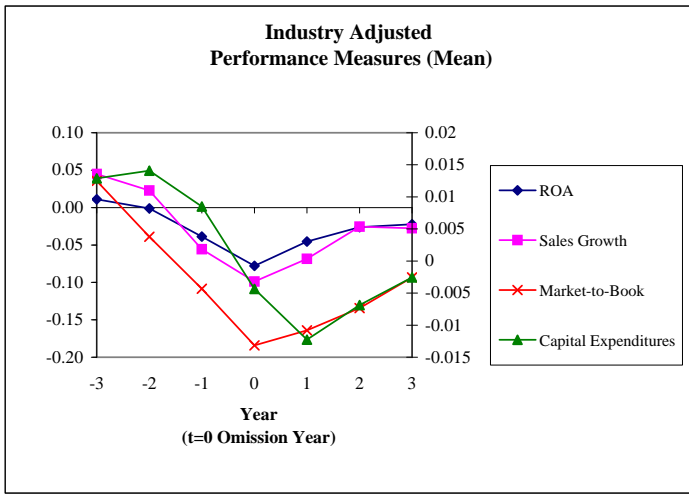


Figure 3: Firm Characteristics of Resumers and Non-Resumers

Key (mean) characteristics of resumers and non-resumers in the seven years centered around the omission year. Resumers are firms that resumed dividend payment within 3 years of the omission year. Non-resumers are firms that never resumed as of 2004 or resumed after 3 years from omission. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the actual firm value.

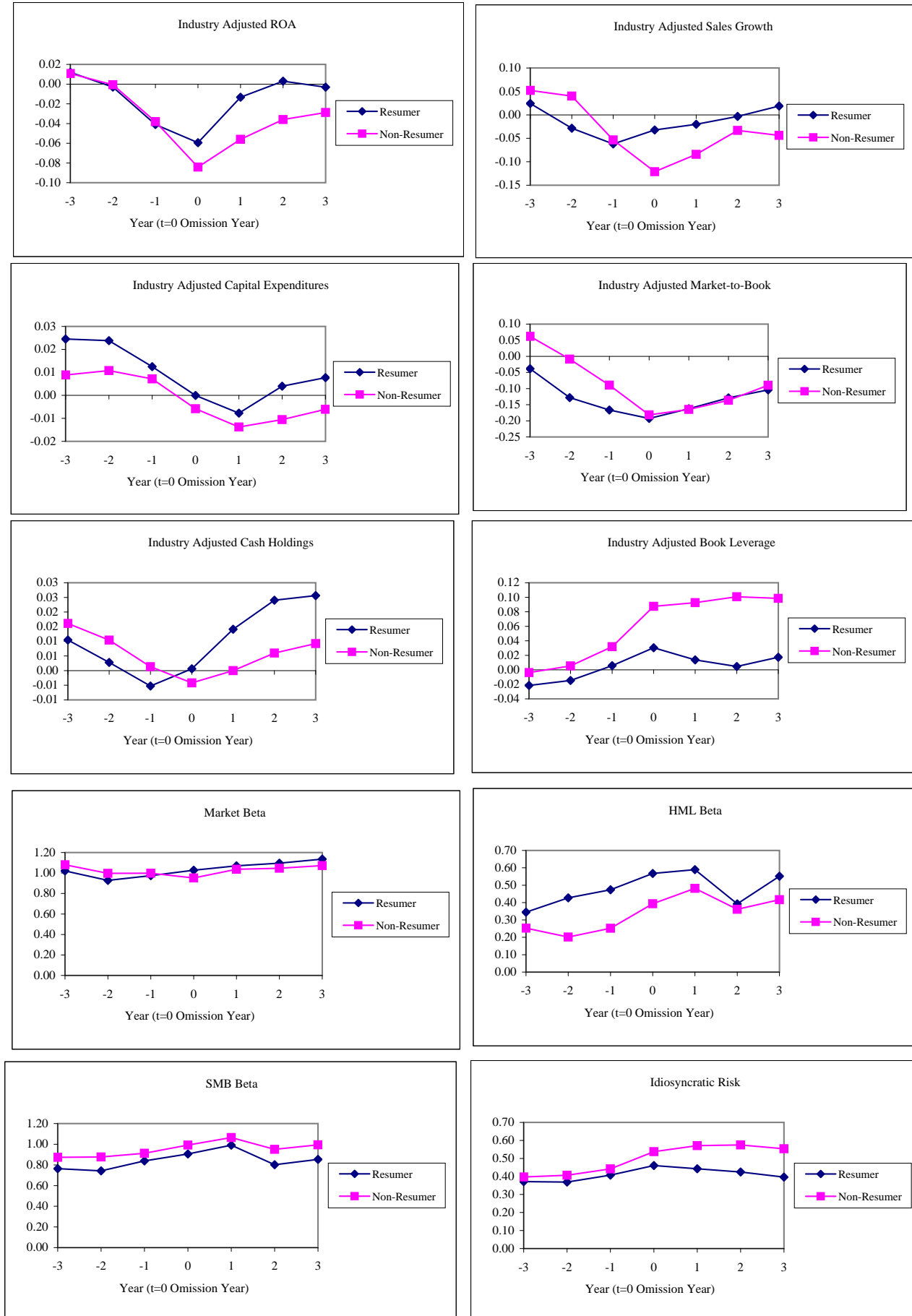


Figure 4: Post-Omission Holding Period Returns for Resumers and Non-Resumers

One, two and three year holding period returns from a buy and hold strategy where the dividend omitting stock is purchased one day after the dividend omission announcement. Excess (market-adjusted) returns are calculated by subtracting the CRSP value-weighted index return over the same period. Resumers are firms that resumed dividend payment within 3 years of the omission. Non-Resumers are firms that never resumed as of 2004 or resumed after 3 years from omission.

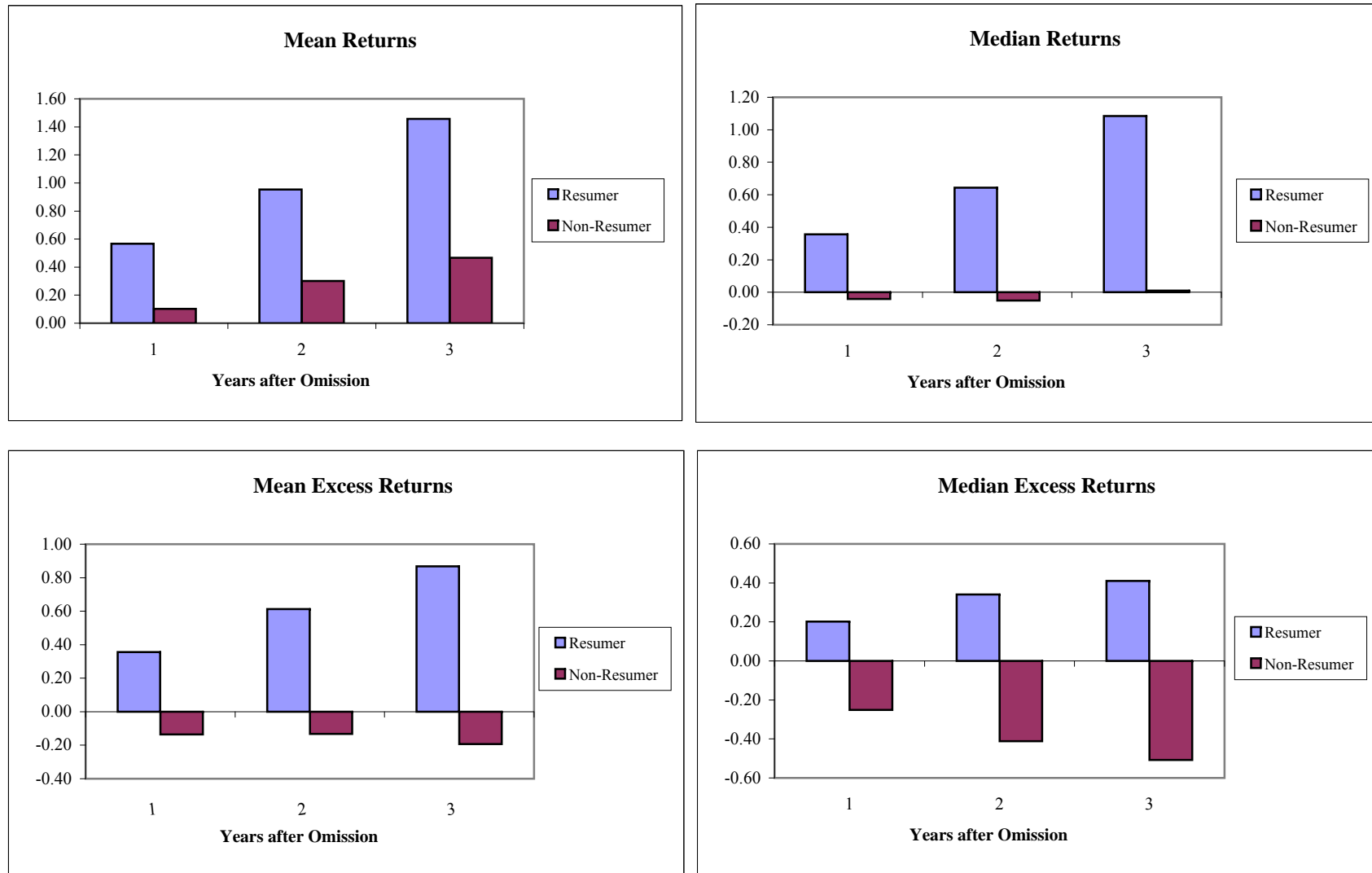


Table I. Dividend Omitting Firms by Year

A dividend omitting firm is defined as a regular cash dividend payer that omits a dividend payment after a minimum of ten years of regular cash dividend payments. A firm is included in the sample if its previous distribution code is 1232, 1242 or 1252, share code is 10 or 11, SIC code is not in the 4900-4999 or 6000-6999 range, and we were able to identify an actual dividend omission announcement date from the *Wall Street Journal Index* or *Lexis-Nexis*.

Year	No. of Omissions	Percentage of all Omissions
1963	2	0.46
1964	1	0.23
1965	2	0.46
1966	2	0.46
1967	6	1.38
1968	4	0.92
1969	10	2.30
1970	35	8.06
1971	18	4.15
1972	10	2.30
1973	5	1.15
1974	12	2.76
1975	17	3.92
1976	8	1.84
1977	9	2.07
1978	8	1.84
1979	13	3.00
1980	27	6.22
1981	21	4.84
1982	35	8.06
1983	10	2.30
1984	10	2.30
1985	13	3.00
1986	23	5.30
1987	10	2.30
1988	8	1.84
1989	11	2.53
1990	15	3.46
1991	16	3.69
1992	14	3.23
1993	9	2.07
1994	6	1.38
1995	6	1.38
1996	7	1.61
1997	2	0.46
1998	6	1.38
1999	8	1.84
2000	1	0.23
2001	7	1.61
2002	4	0.92
2003	2	0.46
2004	1	0.23
Total	434	100

Table II: Descriptive Statistics

Key characteristics of dividend omitting firms in the omission year. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the actual firm value. For the risk measures, the Fama-French betas are estimated using a minimum of 50 daily return observations. Idiosyncratic risk is the annualized standard deviation of residuals from the Fama-French regression. The full sample includes 434 dividend omissions from 1963-2004.

Variable	Mean	Median	Std. Dev.	No. of Obs.
Log Assets (millions)	4.6701	4.5617	1.5646	434
Return on Assets (ROA) - Ind. Adjusted	-0.0780	-0.0697	0.0928	434
Sales Growth - Ind. Adjusted	-0.0989	-0.0966	0.2400	434
Capital Expenditures/Total Assets - Ind. Adjusted	-0.0044	-0.0111	0.0427	434
Market-to-Book Ratio - Ind. Adjusted	-0.1843	-0.2039	0.5348	434
Cash/Total Assets - Ind. Adjusted	-0.0030	-0.0135	0.0713	434
Book Leverage - Ind. Adjusted	0.0733	0.0814	0.2030	434
Market ($R_M - R_f$) Beta	0.9765	0.9491	0.6365	434
SMB (small-minus-big) Beta	0.9637	0.8731	0.8201	434
HML (high-minus-low) Beta	0.4386	0.4068	0.9610	434
Idiosyncratic Risk	0.5186	0.4881	0.2165	434

Table III: Cumulative Abnormal Returns

Cumulative abnormal returns (CARs) are calculated according to the Fama-French three-factor model, measured over the 3-day period centered on the omission announcement date. Cumulative excess returns (CERs) are calculated by subtracting the CRSP value-weighted index return, measured over the 3-day period centered on the omission announcement date. The full sample includes 434 dividend omissions from 1963-2004. Smaller sample sizes are due to missing data. + Significantly different from zero at the 10 % level or better using the t-test for means and Wilcoxon signed-rank test for medians.

Panel A:

Variable	Mean	Median	Std. Dev.	No. of Obs.
3-Day Cumulative Abnormal Return (Fama-French)	-0.0621 +	-0.0566 +	0.0784	430
3-Day Cumulative Excess Return	-0.0656 +	-0.0626 +	0.0797	430

Panel B:

Variable	Mean	Median	Std. Dev.	No. of Obs.	Percent of Omitters
3-Day Cumulative Abnormal Return (Fama-French) >0	0.0409	0.0280	0.0461	84	19.53%
3-Day Cumulative Abnormal Return (Fama-French) <0	-0.0870	-0.0763	0.0627	346	80.47%
3-Day Cumulative Excess Return >0	0.0365	0.0251	0.0519	84	19.53%
3-Day Cumulative Excess Return <0	-0.0904	-0.0799	0.0640	346	80.47%

Table IV: Matched Sample Logit Regressions for a Dividend Omission

Logit analyses of factors affecting the omission decision. The dependent variable equals 1 if the firm is an ommitter and is 0 if a non-ommitter. The table reports marginal effects dP/dx (evaluated at the means), where P is the predicted probability of being an ommitter and x is an explanatory variable. The sample includes 407 ommitters and 407 non-ommitters matched on industry, size and ROA in the year prior to omission. Smaller sample sizes are due to missing data. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the firm's actual value. The explanatory variables are measured in the year before the omission (column 1), as an average of the three years preceding the omission (column 2), as the difference between the future 3-year average and the lagged 3-year average centered on the omission year (column 3), and as the difference between the future 3-year average and the omission year (column 4). Column 4 also includes the lagged 3-year average of the explanatory variables as controls. P values in parentheses are calculated from bootstrapped standard errors (500 repetitions) adjusted to allow for correlation within the two-digit industry group. + significant at 10%; * significant at 5%; ** significant at 1%. # Log assets in columns 3-4 is measured as the lagged 3-year average.

Explanatory Variables	(1)	(2)	(3)	(4)
	Lagged One Year	Lagged 3-year Average	Change	
			From Lagged 3-Year Average	From Omission Year
Log Assets [#] (millions)	-0.0997** 0.000	-0.1075** 0.000	-0.1214** 0.000	-0.0984** (0.000)
Return on Assets (ROA) - Ind. Adjusted %	-0.0125** (0.000)	-0.0052 (0.259)	-0.0017 (0.691)	0.0215** 0.000
Sales Growth - Ind. Adjusted %	0.0008 (0.563)	0.0006 (0.774)	-0.0016 (0.219)	0.0014 (0.316)
Capital Expenditures/Total Assets - Ind. Adjusted %	0.0078* (0.043)	0.0120* (0.020)	-0.0202** (0.002)	-0.0029 (0.675)
Market-to-Book Ratio - Ind. Adjusted %	0.00002 (0.998)	-0.00002 (0.965)	-0.0012 (0.120)	-0.0008 (0.512)
Cash/Total Assets - Ind. Adjusted %	-0.0039 (0.152)	-0.0042 (0.152)	0.0098* (0.011)	0.0113+ (0.060)
Book Leverage - Ind. Adjusted %	0.0044** (0.002)	0.0041* (0.012)	0.0056* (0.011)	0.0027 (0.335)
Market Beta	0.0995* (0.042)	0.1432** (0.009)	0.019 (0.789)	0.1729* (0.022)
SMB Beta	0.0543 (0.121)	0.0333 (0.525)	0.0893+ (0.071)	0.0222 (0.584)
HML Beta	-0.0108 (0.711)	0.0045 (0.917)	-0.0066 (0.861)	-0.0237 (0.555)
Idiosyncratic Risk %	0.0105** 0.000	0.2056** 0.000	0.1131* (0.012)	-0.0225** 0.000
Lagged Variables (3-Year Average) as Controls				Yes
Observations	814	750	602	602
Pseudo R-Square	0.186	0.171	0.175	0.330
Wald Chi-Square	154.7	135.9	88.4	147.6

Table V: Reasons Attached to the Omission Announcement

Reasons provided by firms when announcing a dividend omission. The sample includes 434 firms that omitted dividends between 1963-2004.

	No. of Firms	Percent of all Omitters
None	287	66.1%
Poor Performance	108	24.9%
Strategic Reasons		
To fund current/future investments	13	3.0%
To conserve cash/For financial flexibility	26	6.0%
Total	434	100.0%

Table VI: Dividend Resumptions

Firms that resume regular cash dividend payments x years after a dividend omission. Firms that never resumed are those that have not resumed as of 2004. This includes firms whose stock was delisted after the dividend omission: among these, none were delisted within three years from the omission. The sample includes 434 firms that omitted dividends between 1963-2004.

Year Resumed after Omission	No. of Firms	Percent of all Omitters
Year 1	30	6.9%
Year 2	42	9.7%
Year 3	34	7.8%
After Year 3	117	27.0%
Never Resumed	211	48.6%
Total	434	100.0%

Table VII: Resumers and Non-Resumers - CAR and Dividend History

Resumers are firms that resumed dividend payment within 3 years of the omission. Non-Resumers are firms that never resumed as of 2004 or resumed after 3 years from omission. The last dividend yield prior to omission is Div/P where P is the price 10 days before the omission. The number of dividend cuts in the previous year is weighted by the frequency of dividend payment. The change in the last dividend prior to omission is measured as $(D_j - D_{j-1})/D_{j-1}$ where j is the dividend payment period immediately preceding the omission. The Dividend Premium is derived from Baker and Wurgler (2004) and is the log difference in the market to book ratios of dividend payers and non-payers. + Significantly different from zero at the 10 % level or better using the t-test for means and Wilcoxon signed-rank test for medians. * At least 10 % significance of the t-test of equality of means and the two sample Wilcoxon ranksum test for medians.

Variable	Resumers		Non-Resumers		t Test t-stat	Ranksum Test z-stat
	Mean	Median	Mean	Median		
3-Day Cumulative Abnormal Return (Fama-French)	-0.0606 +	-0.0584 +	-0.0625 +	-0.0566 +	0.2231	-0.0910
3-Day Cumulative Excess Return	-0.0625 +	-0.0570 +	-0.0666 +	-0.0632 +	0.4622	0.2720
Last dividend yield prior to omission	0.0133 +	0.0116 +	0.0125 +	0.0103 +	0.7819	1.084
Number of dividend cuts in previous 3 years	0.6667 +	1 +	0.8930 +	1 +	-1.4699	-0.748
Change in last dividend prior to omission	-0.0678 +	0 +	-0.0399 +	0 +	-0.8415	-0.943
Dividend Premium in Omission Year	-2.8493 +	-6.30 +	-5.3723 +	-7.80 +	1.4785	0.8440

Table VIII: CAR Regressions for Resumers and Non-Resumers

Cumulative abnormal returns (CAR) are calculated according to the Fama-French three-factor model, measured over the 3-day period centered on the omission announcement date. Cumulative excess returns are calculated by subtracting the CRSP value-weighted index return measured over the 3-day period centered on the omission announcement date. Resumers are firms that resumed dividend payment within 3 years of the omission. Non-Resumers are firms that never resumed as of 2004 or resumed after 3 years from omission. The resumer dummy equals one if the firm is a resumer and is zero otherwise. The full sample includes 434 dividend omissions from 1963-2004. Smaller sample sizes are due to missing dividend history data or missing daily price data. The last dividend yield prior to omission is Div/P where P is the price 10 days before the omission. The number of dividend cuts in the previous year is weighted by the frequency of dividend payment. The change in the last dividend prior to omission is measured as $(D_j - D_{j-1})/D_{j-1}$ where j is the dividend payment period immediately preceding the omission. The Dividend Premium is derived from Baker and Wurgler (2004) and is the log difference in the market to book ratios of dividend payers and non-payers. Estimation is by OLS with bootstrapped standard errors (500 repetitions) adjusted to allow for correlation within the two-digit SIC industry group. + significant at 10%; * significant at 5%; ** significant at 1%.

	Dependent Variable			
	Fama-French CAR		Cumulative Excess Return	
	(1)	(2)	(3)	(4)
Explanatory Variables				
Resumer Dummy	0.007 (0.412)	0.007 (0.428)	0.009 (0.255)	0.009 (0.260)
Last dividend yield prior to omission	-1.1494* (0.011)	-1.1447* (0.014)	-1.2093** (0.005)	-1.1981** (0.006)
Number of dividend cuts in previous 3 years	0.0051+ (0.058)	0.0051+ (0.070)	0.0057* (0.027)	0.0058* (0.037)
Change in last dividend prior to omission	0.0052 (0.484)	0.0053 (0.491)	0.0058 (0.428)	0.0058 (0.432)
Dividend Premium	-0.0006* (0.012)	-0.0006** (0.009)	-0.0007** (0.004)	-0.0007** (0.005)
Omission Explanation Dummies:				
For strategic reasons	0.011 (0.194)		0.013 (0.107)	
To fund current/future investments		0.015 (0.281)		0.0219+ (0.059)
To preserve financial flexibility		0.008 (0.396)		0.008 (0.369)
Constant	-0.0574** (0.000)	-0.0575** (0.000)	-0.0619** (0.000)	-0.0622** (0.000)
Observations	425	425	425	425
Adjusted R-squared	0.029	0.027	0.036	0.035

Table IX: Logit Regressions for the Type of Omitter I

Logit analyses of factors affecting the type of ommitter. The dependent variable = 1 if the firm is a resumer and = 0 if the firm is a non-resumer. The table reports marginal effects dP/dx evaluated at the means, where P is the predicted probability of being a resumer and x is an explanatory variable. Resumers are firms that resumed dividend payment within 3 years of the omission. Non-Resumers are firms that never resumed as of 2004 or resumed after 3 years from omission. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the firm's actual value. The Dividend Premium is derived from Baker and Wurgler (2004) and is the log difference in the market to book ratios of dividend payers and non-payers. The omission explanation dummy equals one if the omitting firm provides an explanation for the omission. Explanatory variables are measured in the year of the omission (columns 1-2), in the year before the omission (columns 3-4), as an average of the three years preceding the omission (columns 5-6), as the difference between the future 3-year average and the lagged 3-year average centered on the omission year (column 7), and as the difference between the future 3-year average and the omission year (column 8). Column 8 also includes the lagged 3-year average of the explanatory

The full sample includes 434 dividend omissions from 1963-2004. Smaller sample sizes are due to missing data. P values in parentheses are calculated from bootstrapped standard errors (500 repetitions) adjusted to allow for correlation within the two-digit SIC industry group. + significant at 10%; * significant at 5%; ** significant at 1%.

[#]In columns 7-8, log assets is measured as the lagged 3-year average while the dividend premium is measured in the year of omission.

Explanatory Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7) (8)	
	Year of Omission	Year of Omission	Lagged One Year	Lagged One Year	Lagged 3-year Average	Lagged 3-year Average	Change	
							From Lagged 3-Year Average	From Omission Year
Log Assets [#] (millions)	0.0293+ (0.054)	0.0289+ (0.056)	0.0465** (0.002)	0.0480** (0.003)	0.0182 (0.313)	0.0203 (0.251)	0.0119 (0.394)	0.023 (0.254)
Return on Assets (ROA) - Ind. Adjusted %	0.0038 (0.132)	0.0036 (0.179)	-0.0009 (0.775)	-0.0007 (0.827)	0.0021 (0.617)	0.0023 (0.572)	0.0042 (0.275)	0.0072* (0.038)
Sales Growth - Ind. Adjusted %	0.0027* (0.028)	0.0031* (0.025)	-0.0002 (0.840)	-0.0002 (0.998)	-0.0035* (0.022)	-0.0035* (0.016)	0.0028** (0.008)	-0.0007 (0.453)
Capital Expenditures/Total Assets - Ind. Adjusted %	0.0051 (0.353)	0.0051 (0.298)	0.0080+ (0.067)	0.0081* (0.035)	0.0167** (0.001)	0.0168** (0.000)	-0.0079 (0.147)	0.0049 (0.423)
Market-to-Book Ratio - Ind. Adjusted %	-0.0003 (0.658)	-0.0003 (0.585)	-0.0004 (0.372)	-0.0004 (0.359)	-0.0005 (0.336)	-0.0005 (0.306)	0.0004 (0.591)	-0.0007 (0.487)
Cash/Total Assets - Ind. Adjusted %	0.0014 (0.689)	0.0014 (0.666)	-0.0043 (0.173)	-0.004 (0.214)	-0.0003 (0.935)	-0.0002 (0.953)	0.0056+ (0.060)	0.0054 (0.240)
Book Leverage - Ind. Adjusted %	-0.0036** (0.002)	-0.0036** (0.002)	-0.0041** (0.008)	-0.0040* (0.012)	-0.0027 (0.121)	-0.0027 (0.111)	-0.0046* (0.039)	-0.0035 (0.164)
Market Beta	0.0275 (0.535)	0.0399 (0.363)	-0.0725+ (0.093)	-0.0717+ (0.089)	-0.0124 (0.819)	-0.0099 (0.855)	0.1095+ (0.085)	-0.0111 (0.843)
SMB Beta	0.0039 (0.878)	-0.0012 (0.960)	0.0204 (0.551)	0.021 (0.531)	-0.0665 (0.192)	-0.0669 (0.203)	-0.0047 (0.916)	0.0004 (0.988)
HML Beta	0.0174 (0.504)	0.0165 (0.505)	0.0859** (0.002)	0.0860** (0.002)	0.1294** (0.001)	0.1352** (0.001)	-0.0188 (0.613)	-0.0045 (0.888)
Idiosyncratic Risk %	-0.0041** (0.000)	-0.0041** (0.000)	-0.0016 (0.186)	-0.0015 (0.206)	-0.0399 (0.128)	-0.0367 (0.167)	-0.1237** (0.000)	0.0061** (0.002)
Dividend Premium [#]	0.0025+ (0.053)	0.0023+ (0.088)	0.0029+ (0.061)	0.0028+ (0.081)	0.0034* (0.028)	0.0032+ (0.051)	0.0028+ (0.059)	0.0040* (0.021)
Omission Explanation Dummy		-0.0927* (0.018)		-0.0718+ (0.084)		-0.0762+ (0.074)	-0.0424 (0.342)	-0.0796 (0.112)
Lagged Variables as Controls								Yes
Observations	434	434	431	431	404	404	367	367
Pseudo R-Square	0.095	0.105	0.062	0.067	0.089	0.095	0.160	0.156
Wald Chi-Square	38.44	36.77	31.50	32.75	34.43	38.28	27.48	44.94

Table X: Cash Saved, Financial Flexibility and Investment Policy

Cash saved is the annualized dollar value of the cash dividend payment immediately preceding the omission scaled by total assets. Debt overhang is the firm's industry adjusted book leverage ratio. The reduction in book leverage (debt overhang) is the difference between the omission year value and the one-year post-omission value of this variable. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the actual firm value. Resumers are firms that resumed dividend payment within 3 years of the omission. Non-Resumers are firms that never resumed as of 2004 or resumed after 3 years from omission. The full sample includes 434 dividend omissions from 1963-2004. Smaller sample sizes are due to missing data. + Significantly different from zero at the 10 % level or better using the t-test for means and Wilcoxon signed-rank test for medians. * At least 10 % significance of the t-test for equality of means and the two sample Wilcoxon ranksum test for medians.

Variable	Resumer		Non-Resumer		t Test	Ranksum Test
	Mean	Median	Mean	Median	t-stat	z-stat
Cash Saved from the Omission and Debt Overhang						
Cash Saved from the Omission (millions)	4.8156 +	1.6532 +	4.7506 +	0.9054 +	-0.253	2.032 *
Cash Saved from the Omission/Total Assets	0.0149 +	0.0122 +	0.0144 +	0.0099 +	-0.6555	0.046
Debt Overhang in Omission Year (millions)	34.4933 +	3.0864 +	84.7921 +	5.7574 +	-1.5178	-1.981 *
Debt Overhang in Omission Year/Total Assets	0.0304 +	0.0426 +	0.0875 +	0.0864 +	-2.548 *	-2.663 *
Cash Saved - Debt Overhang in Omission Year (millions)	-29.6777 +	-1.9325 +	-80.0416 +	-4.7343 +	-0.2321	2.055 *
Cash Saved - Debt Overhang in Omission Year/Total Assets	-0.0155	-0.0209	-0.0731 +	-0.0772 +	2.4748 *	2.617 *
Reduction in Book Leverage after the Omission Year	0.0242 +	0.0245 +	-0.0035	0.0003	2.5823 *	3.597 *
Reduction in Debt Overhang after the Omission Year/Total Assets	0.0170 +	0.0226 +	-0.0077	-0.0039	2.2163 *	3.278 *
Financial Flexibility After the Omission						
Cash Holdings/Total Assets (3 year Forward Average)	0.0873 +	0.0679 +	0.0736 +	0.0452 +	1.4666	2.605 *
Cash Holdings/Total Assets (3 year Forward Average) - Industry Adj.	0.0220 +	0.0069 +	0.0041	-0.0068	1.969 *	2.672 *
Book Leverage (3 year Forward Average)	0.4861 +	0.4948 +	0.5671 +	0.5636 +	-3.3201 *	-3.693 *
Debt Overhang (3 year Forward Average)/Total Assets	0.0105	0.0033	0.0947 +	0.0880 +	-3.4599 *	-3.71 *
Investment Policy After the Omission						
Capital Expenditures/Total Assets (3 year Forward Average)	0.0573 +	0.0496 +	0.0474 +	0.0370 +	2.1842 *	3.376 *
Capital Expenditures/Total Assets (3 year Forward Average) - Industry Adj.	0.0014	-0.0010	-0.0097 +	-0.0154 +	2.7742 *	4.29 *
Market-to-Book Ratio (3 year Forward Average)	0.9758 +	0.9199 +	1.0523 +	0.9425 +	-1.4629	-0.968
Market-to-Book Ratio (3 year Forward Average) - Industry Adj.	-0.1314 +	-0.1379 +	-0.1312 +	-0.1768 +	-0.003	1.224

Table XI: Logit Regressions for the Type of Omitter II

Logit analyses of factors affecting the type of ommitter. The dependent variable = 1 if the firm is a resumer and = 0 if the firm is a non-resumer. The table reports marginal effects dP/dx , where P is the predicted probability of being a resumer and x is an explanatory variable. Resumers are firms that resumed dividend payment within 3 years of the omission. Non-resumers are firms that never resumed as of 2004 or resumed after 3 years from omission. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the firm's actual value. The Dividend Premium is derived from Baker and Wurgler (2004) and is the log difference in the market to book ratios of dividend payers and non-payers. The omission explanation dummy equals one if the omitting firm provides an explanation for the omission. The pre- (post-)omission management turnover dummy equals one if at least one of the top three executives was replaced in the year before (after) the omission. The number of dividend cuts in the last three years is weighted by the frequency of dividend payment. Explanatory variables are measured in the year of the omission (columns 1-2), in the year before the omission (columns 3-4), as an average of the three years preceding the omission (columns 5-6), as the difference between the future 3-year average and the lagged 3-year average centered on the omission year (column 7), and as the difference between the future 3-year average and the omission year (column 8). Column 8 also includes the lagged 3-year average of the explanatory variables as controls. The full sample includes 434 dividend omissions from 1963-2004. Smaller sample sizes are due to missing data. P values in parentheses are calculated from bootstrapped standard errors (500 repetitions) adjusted to allow for correlation within the two-digit SIC industry group. + significant at 10%; * significant at 5%; ** significant at 1%. #In columns 7-8, log assets is measured as the lagged 3-year average while the dividend premium is measured in the year of omission. ###We find similar effects when we include the post-omission turnover dummy in columns 1-6.

Explanatory Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7) (8)	
	Year of Omission		Lagged One Year		Lagged 3-year Average		Change	
							From Lagged 3-Year	From Omission Year
Log Assets [#]	0.0277+ (0.066)	0.0301+ (0.067)	0.0464** (0.005)	0.0476** (0.005)	0.0184 (0.310)	0.0184 (0.329)	0.0185 (0.198)	0.0234 (0.286)
Return on Assets (ROA) - Ind. Adjusted %	0.0037 (0.158)	0.003 (0.270)	-0.0003 (0.941)	-0.0009 (0.776)	0.0033 (0.463)	0.0027 (0.538)	0.0053 (0.177)	0.0072* (0.040)
Sales Growth - Ind. Adjusted %	0.0030* (0.025)	0.0029* (0.026)	-0.00004 (0.973)	-0.00001 (0.993)	-0.0037* (0.022)	-0.0037* (0.018)	0.0027** (0.010)	-0.0007 (0.447)
Capital Expenditures/Total Assets - Ind. Adjusted %	0.0051 (0.295)	0.0053 (0.317)	0.0082* (0.049)	0.0078+ (0.078)	0.0170** (0.001)	0.0172** (0.001)	-0.0076 (0.137)	0.0049 (0.490)
Market-to-Book Ratio - Ind. Adjusted %	-0.0003 (0.590)	-0.0003 (0.633)	-0.0005 (0.367)	-0.0004 (0.365)	-0.0005 (0.325)	-0.0005 (0.329)	0.0002 (0.798)	-0.0007 (0.513)
Cash/Total Assets - Ind. Adjusted %	0.0009 (0.800)	0.0011 (0.761)	-0.0046 (0.180)	-0.0046 (0.204)	-0.0004 (0.911)	-0.0005 (0.887)	0.0057+ (0.079)	0.0058 (0.202)
Book Leverage - Ind. Adjusted %	-0.0038** (0.003)	-0.0040** (0.002)	-0.0042* (0.010)	-0.0044** (0.007)	-0.0028 (0.130)	-0.0031+ (0.086)	-0.0047* (0.036)	-0.0034 (0.196)
Market Beta	0.0418 (0.346)	0.0434 (0.326)	-0.0697 (0.122)	-0.0681 (0.162)	-0.0077 (0.889)	-0.0041 (0.941)	0.0944 (0.129)	-0.0132 (0.825)
SMB Beta	-0.0014 (0.958)	-0.0008 (0.975)	0.0185 (0.573)	0.0184 (0.570)	-0.0676 (0.205)	-0.0766 (0.137)	0.0048 (0.914)	-0.0016 (0.958)
HML Beta	0.0191 (0.472)	0.0197 (0.452)	0.0857** (0.004)	0.0834** (0.003)	0.1350** (0.001)	0.1369** (0.001)	-0.0159 (0.647)	0.0018 (0.953)
Idiosyncratic Risk %	-0.0040** (0.000)	-0.0040** (0.002)	-0.0014 (0.292)	-0.0013 (0.326)	-0.0368 (0.208)	-0.0362 (0.184)	-0.1214** (0.000)	0.0057** (0.005)
Dividend Premium [#]	0.0022 (0.142)	0.0021 (0.152)	0.0026+ (0.090)	0.0026 (0.108)	0.0030+ (0.075)	0.0030+ (0.078)	0.0029+ (0.055)	0.0039* (0.031)
Omission Explanation Dummy	-0.0942* (0.014)	-0.0889* (0.024)	-0.0740+ (0.072)	-0.0681 (0.112)	-0.0802+ (0.074)	-0.0746+ (0.097)	-0.0546 (0.184)	-0.0873+ (0.056)
Pre-Omission Management Turnover Dummy	-0.0094 (0.868)	-0.0173 (0.771)	-0.0209 (0.721)	-0.0300 (0.622)	-0.0342 (0.592)	-0.0454 (0.478)	-0.0173 (0.790)	-0.0352 (0.652)
Post-Omission Management Turnover Dummy ^{###}							-0.1109* (0.018)	-0.0959+ (0.080)
Number of dividend cuts in previous 3 years		-0.0357+ (0.085)		-0.0373+ (0.057)		-0.0496* (0.016)	-0.0269 (0.274)	-0.0414 (0.145)
Lagged Variables as Controls								Yes
Observations	429	429	426	426	399	399	364	364
Pseudo R-Square	0.105	0.110	0.067	0.074	0.096	0.107	0.175	0.169
Wald Chi-Square	33.31	34.49	31.82	32.71	40.58	41.81	31.44	48.43

Table XII: Determinants of Dividend Resumptions Soon After an Omission

Column 1: Cox proportional hazard analysis of factors affecting a dividend resumption within 3 years from the omission. The dependent variable equals one if the firm resumes dividend payment in a particular year; otherwise it is zero. The sample is right-censored after three years from the omission. To mitigate problems of attrition, we artificially right-censor observations of firms that were delisted within 3 years from omission by dropping their last firm-year observation in the sample. The table reports hazard ratios e^{β} , i.e. a unit change in covariate x results in an $(e^{\beta}-1)$ percent change in the probability of resumption. Distinct baseline hazards are estimated for each 2-digit SIC group.

Column 2: Logit analyses of factors dividend resumptions within 3 years from omission. The dependent variable equals one if the firm resumes dividend payment within 3 years from omission; it is zero if the firm resumes dividend payment more than 3 years after omission but before our sample period ends in 2004. The table reports marginal effects dP/dx evaluated at the means, where P is the predicted probability of being a dividend resumer within 3 years from omission. Columns 1 and 2: Explanatory variables are lagged one year from resumption. Industry adjusted variables are calculated by subtracting the variable's annual 2-digit SIC median value from the firm's actual value. The Dividend Premium is derived from Baker and Wurgler (2004) and is the log difference in the market to book ratios of dividend payers and non-payers. The full sample includes 434 dividend omissions from 1963-2004. Smaller sample sizes are due to missing data. P values in parentheses correspond to bootstrapped standard errors (500 repetitions) adjusted for correlation within the two-digit SIC industry group. + significant at 10%; * significant at 5%; ** significant at 1%.

Explanatory Variables	(1)	(2)
	Hazard Model	Logit Model
Log Assets (millions)	1.1242 (0.265)	0.0683* (0.049)
Return on Assets (ROA) - Ind. Adjusted %	1.0421+ (0.052)	-0.0197** (0.002)
Sales Growth - Ind. Adjusted %	1.003 (0.676)	-0.0046* (0.039)
Capital Expenditures/Total Assets - Ind. Adjusted %	0.9961 (0.908)	0.008 (0.453)
Market-to-Book Ratio - Ind. Adjusted %	0.9974 (0.504)	0.0006 (0.577)
Cash/Total Assets - Ind. Adjusted %	1.007 (0.715)	-0.008 (0.163)
Book Leverage - Ind. Adjusted %	0.9850+ (0.058)	-0.0032 (0.205)
Market Beta	0.9111 (0.749)	-0.0561 (0.532)
SMB Beta	0.9844 (0.932)	-0.1067+ (0.074)
HML Beta	0.9383 (0.701)	0.0965+ (0.055)
Idiosyncratic Risk %	0.9815* (0.019)	0.0005 (0.836)
Dividend Premium	1.0201* (0.025)	-0.003 (0.293)
Observations	1191	220
Number of Resumers	88	110
Number of Firms	430	220
Pseudo R-Square	0.059	0.142
Log-Likelihood	-208.3	
Wald Chi-Square		31.2