

Management Quality, Financial Policies, and Performance of Seasoned Equity Issuers

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Abstract

Using a unique sample of hand-collected data on the management quality of firms making seasoned equity offerings (SEO), we examine the relationship between the reputation and quality of a firm's management and its financial policies, SEO characteristics, and post-SEO performance, a relationship that has so far received little attention in the literature. We hypothesize that better and more reputable managers are able to convey the intrinsic value of their firm more credibly to outsiders, thus reducing the information asymmetry facing their firm in the equity market. Given this, such firms will have more access to the equity market, so that we expect lower leverage ratios for these firms. In addition, they will have less need to signal using dividends, so that they will have lower dividend payout ratios. Further, given that financial intermediaries like investment banks and institutional investors will incur lower costs of producing information about such firms, we expect firms with better and more reputable managements to be associated with more reputable underwriters, smaller underwriting expenses, and larger institutional holdings. Further, since better managers are likely to select better projects (having a higher NPV for any given scale) and implement them more ably, higher management quality will also be associated with larger SEO offer sizes, higher levels of investment and R&D expenditures, and better post-SEO operating performance. We present evidence consistent with the above hypotheses.

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