Dividends and Debt in Pyramidal Structures: Evidence from France

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Draft: 30 May 2008

The authors appreciate the helpful comments from Daniel Wolfenzon and T.J. Wong, as well as from participants at The Institute for Corporate Governance at Chinese University of Hong Kong, The Law and Economics Center at Tilburg University, and the Corporate Governance Symposium at the 2008 European Accounting Association. The authors acknowledge the able and extensive research assistance provided by Sereeparp Anantanvrasilp.

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Abstract

This paper analyzes the impact of large shareholders and control-enhancing mechanisms on payout policy by exploring pyramidal structures in France. We closely scrutinize the use of debt in holding companies and its role as a control-enhancing mechanism. We document that, in France, debt in holding companies constitutes a dominant part of the overall discrepancy between control and cash flow rights (the control wedge). We find that the dividend payout decreases in the control wedge, in accordance with the Expropriation Hypothesis of La Porta et al. (2000). However, we also find that the use of pyramidal structures can increase payouts to shareholders, echoing earlier findings on European companies. By including the financial structure adopted in the holding companies, we can help resolve this apparent contradiction. Specifically, we present evidence that the use of debt in holdings can act as a commitment device that favors larger dividend payouts.

A second contribution is our analysis of the actual dividend payouts to controlling owners along the pyramidal chain, in contrast to earlier pyramid studies that only considered potential payouts. We find that only a fraction of the cash made available to controlling owners is actually paid out to them.