

## Corporate Finance, Module 15, “Common Stock Dividends”

*Required reading:*

(The attached PDF file has better formatting.)

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{The Brealey and Myers textbook is excellent. We say to read certain sections and to skip others. This does not mean that certain sections are better; it means that the homework assignments and exam problems are based on the sections that you must read for this course. Some of the skipped sections are fascinating, but they are not tested.}

Read the boxed introduction on page 433. As Brealey and Myers say, the central question is “How does dividend policy affect firm value?”

Read section 16.1, “How Dividends Are Paid,” on pages 433-436. These are facts about dividends; even if you know how stocks are traded, the section on stock repurchase plans contains much new information.

Skip section 16.2, “How Do Companies Decide on Dividend Payments,” on pages 437-438. We don’t need Lintner’s model for the financial theory in this textbook. The model is reasonable, but it is not used elsewhere in this course.

Read section 16.3, “The Information in Dividends and Stock Repurchases,” on pages 438-441, skipping “The Dividend Cut Heard Round the World” on page 440. Many common dividend practices are hard to explain, and financial analysts presume that dividends send information to investors, not just money. There are more efficient ways of getting money to investors, but dividends may be a good source of information.

Read section 16.4, “The Dividend Controversy,” on pages 441-447, focusing on the subsection “Dividend Policy Is Irrelevant in Perfect Capital Markets” on pages 442-443. You will find the illustration on page 444 helpful for understanding the theory and answering final exam questions. Understanding this irrelevance theorem is important; the irrelevance theorem for capital structure is similar, so spend time to make sure you grasp the concept.

Skip section 16.5, “The Rightists,” on pages 447-448; skip section 16.6, “Taxes and the Radical Left,” on pages 448-452; and skip section 16.7, “the Middle-of-the-Roaders,” on pages 452-455. Brealey and Myers are middle-of-the-roaders. But financial analysts differ so much in their views of dividends that Brealey and Myers present the full range of current opinion. If you trade common stocks, you may want to read these sections to better judge how dividends affect your stock values, but these sections are not tested on the final exam.

Read the summary on page 455, stopping at the second line from the top on page 456: “... to run a tighter ship”; skip the rest of the summary.