WRONG QUESTIONS, WRONG METHOD? - PRELIMINARY EVIDENCE ON THE POTENTIAL FOR INTERVIEW AND SMALL SAMPLE RESEARCH TO EXPLAIN FIRMS' EQUITY FINANCING CHOICES.

By

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1. Introduction

In this study we report the results of discussions with fund managers about UK firms' equity issuing behaviour; these discussions formed the basis for a large number of ongoing interviews with firms which have recently made seasoned equity issues (SEOs). In this paper we discuss why we believe such a preliminary study is necessary. The study will enable us to ascertain the factors which the interviewees suggest are an important influence on how companies approach equity fund raising in practice and which should, therefore, form the basis of our subsequent discussions with issuing firms. The interview material also highlights a number of reasons why conventional large-scale empirical analysis may not represent an appropriate avenue for establishing firms' motivations for using different financing methods.

The next section of the paper discusses the existing literature about firms decisions to issue equity. It indicates the problems that arise from the concentration of various studies on large sample aggregate analysis and describes the potential for case study and face-to-face research to inform the debate. The third section of the paper describes the interview process and re-emphasises how it fits into our wider research plan before the fourth section details our discussions. The fifth section outlines the main implications of the interview material, while the final section of the paper offers some preliminary conclusions, particularly in terms of the implications of this study for future investigations of corporate fund raising activities.

2. Background to the Study

Some of the best documented results to emerge from the modern finance literature relate to the stock market reaction to announcements about issues of new securities. However, despite the consistency in the empirical evidence, the findings pose a number of interesting questions for researchers, few of which have been resolved satisfactorily on the basis of the large sample aggregate analyses which dominate the area. The best known evidence relating to financing disclosures relates to the short-term market response to news of forthcoming share issues by companies that are already listed on a stock market - SEOs. Two-day market-adjusted returns following such disclosures are almost always negative, significantly different from zero, and in the region of -3%; in contrast, disclosures about debt issues appear to exert no significant influence on share prices (see e.g. Asquith and Mullins, 1986; Masulis and Korwar, 1986; Healy and Palepu, 1990; Sant and Ferris, 1994).[1]

Consistent patterns in longer term price movements around SEO announcements have also been reported by Affleck-Graves and Page (1995), Loughran and Ritter (1995), Speiss and Affleck-Graves (1995) and Jung et al. (1996). The studies all report that equity issues are followed by long-term average price declines that persist for up to 5 years after the offer is made; for example, Loughran and Ritter (1995) show that the return for equity-issuing firms over a five-year period is 33% while the return earned by a matched sample of non-issuers is 93% over the same period. In addition, Korajczyk et al. (1990) and Asquith and Mullins (1986) both report that equity issues tend to follow periods of sustained abnormal price gains and the evidence as a whole therefore suggests that equity issues are made during long-term peaks in share prices.

Academics have identified a number of possible rationales for the market reaction to new financing announcements and these have been usefully grouped into three categories by Barclay and Litzenberger (1988). The authors identify theories based on (i) information / signalling issues, where the negative reaction to SEO announcements occurs because investors believe that an equity issue signifies managers' belief that the shares are overpriced and / or that the proceeds provide the opportunity for wasteful investment on projects with negative net present values, (ii) price pressure arguments which suggest that the adverse response to an increase in the supply of shares is axiomatic because of a downward sloping demand curve for corporate equity and (iii)

[1] See Smith (1986), Armitage (1998) and Burton et al. (2000) for detailed reviews of the evidence concerning the market reaction to SEOs.

gearing hypotheses, based on the idea that the market reaction to a new financing announcement represents a response to an accompanying change in the weighted average cost of capital.

A body of empirical evidence about cross-sectional variation in the market reaction to SEOs has also developed, partly as an attempt to test the predictions of the theories. The many variables studied to date include operating performance (Loughran and Ritter, 1995), company size (Kalay and Shimrat, 1987), growth prospects (Pilotte, 1992; Burton et al., 2000), issue purpose (Masulis and Korwar, 1986), return variability (Mann and Sicherman, 1991) and earnings management (Teoh et al., 1998). These studies, all of which are based on large-sample regression analysis, show that while the explanations outlined by Barclay and Litzenberger may be theoretically sound, no single model is consistent with all the evidence. For example, (i) the information hypotheses predict a straight forward positive reaction to debt issues, but this has never been found in practice, (ii) the theories based on the price pressure arguments are entirely consistent with the short-term market reaction to SEOs yet they provide no explanation for the long term gains (falls) prior to (following) the announcements and (iii) the gearing hypothesis predicts a simple positive relationship between issue size and the market response to an SEO - the evidence on this remains inconclusive (see, e.g. Asquith and Mullins, 1986; Dierkins, 1991).

The studies that examine the market reaction to SEOs are, however, based almost entirely on large sample analyses and so the reasons why individual firms issue equity in practice are not fully known. This failure to incorporate heterogeneity in firms' motives for issuing equity is arguably one of the main reasons why a comprehensive explanation of share price movements around new financing announcements does not yet exist; this question clearly lends itself to a move away from aggregate analysis to instead study individual firm behaviour and their motives for issuing equity.

Related attempts to derive theoretical explanations for firms' decisions about whether to issue debt or equity (and, by inference, their target capital structure) have also proved relatively unsuccessful. In particular, no theory has been devised which fully explains why firms continue to use SEOs in the face of mounting evidence that the announcement of a forthcoming share issue reduces shareholder wealth in both the short- and long-run. The case for examining why large companies choose a particular form of new financing by communicating directly with issuing firms would seem to be overwhelming and yet few studies have been undertaken on this basis.[2] Possibly as a result of this omission, apparently sound theories exist to explain corporate financing activity, but again no model is consistent with all the evidence. The two dominant explanations in the extant literature are (i) *static-trade off theory* (see e.g. Myers, 1984), which explains corporate financing activity in terms of movements towards a target capital structure, with the target itself being derived by balancing the tax benefits of debt financing with the financial distress costs incurred at high gearing levels and (ii) *pecking order theory* (e.g. Myers and Majluf, 1984). The model predicts that firms finance investment according to the relative costs of alternative methods with retained earnings being preferred, followed by debt and then equity. External fund raising activity is therefore not driven by any target capital structure, but instead reflects gaps between internal funds and investment opportunities (net of dividends), as well as the extent of divergences between the market and intrinsic values of corporate securities.

Empirical evidence exists to support these two broadly based theories; for example, the findings of both Marsh (1982), who reports the existence of long term target gearing levels for UK firms, and Long and Malitz (1985) who discover significant negative relationships between intangible assets and gearing levels in the US, support the static-trade off model. However Choe et al. (1993) and Bayless and Chaplinsky (1996) find that firms prefer to issue equity at times when shares are relatively overpriced (i.e. when the market value of equity is relatively close to the intrinsic value) and thereby provide a measure of support for pecking order theory. The picture which emerges from the large sample tests of capital structure theories is further complicated by the suggestion in Shyam-Sunder and Myers (1999) that the static trade-off and

[2] In contrast to the situation regarding fund raising behaviour, interviews and questionnaires have always played a key role in attempts to understand the motivations behind firms' dividend decisions (see e.g. Lintner, 1956 and

pecking order theories overlap to a degree; the practical implication of their analysis is that empirical evidence which appears at first glance to offer support for the static trade-off model may not be inconsistent with a pecking order-based model of corporate gearing choice.

One of the few studies to move beyond large sample analysis in its investigation of corporate financing behaviour is Pinegar and Wilbricht (1989). Their evidence illustrates the potential for case study and small sample research to yield insights into corporate decision making beyond those achieved via conventional aggregate analysis and *a priori* theorising. The authors employ a questionnaire survey of *Fortune 500* firms in 1986 (receiving 176 useable replies) and conclude that managerial responses are consistent with the broad predictions of pecking order theory. The sample firms express a clear preference for internal funding over external funding and for debt financing rather than share issues. In addition, answers to a series of questions about the factors which influence financing behaviour show that variables which play a major part in the static trade-off theory - tax and bankruptcy considerations - are not seen as being important by the managers of large US firms.

A number of other unresolved puzzles exist regarding corporate equity issues; in particular, US firms are now known to favour fully underwritten offers and make little or no use of rights issues despite the widely acknowledged evidence that rights issues are the cheapest SEO vehicle method available to American firms (see e.g. Smith, 1977; Hansen, 1988; Eckbo and Masulis, 1992). Although no similar differences in issue costs have yet been uncovered in the UK, this 'rights offer paradox' appears to suggest that major companies' choice of issue method is determined by something other than the cost of the issue; these costs are, however, ultimately borne by the equity holders, again suggesting that firms' voluntary fund raising behaviour causes harm to existing shareholders.[3]

Baker et al., 1985).

[3] Patterson and Ursel (1993) find further 'irrationality' with firms preferring to pay for underwritten rather than guaranteeing success through deep-discounting, according to the authors because of perceived dilution because of the discount involved with rights issues.

The apparently anomalous findings about the role of issue costs may partly be explained by the relative dearth of information about the decision processes that companies go through when deciding on equity issue methods. Very little work has been undertaken to establish the costs of alternative methods of share issuance, although Armitage (2000) finds no evidence of significant differences in the total cost of rights and open offers in the UK[4]. The focus of the existing literature has traditionally been on the costs associated with the secondary trading of shares once they have been issued. For example, the National Association of Security Dealers (NASD) and their automated quotation market (NASDAQ) have been subject to Department of Justice investigations and fines in excess of $1billion because of their large transaction costs. As far back as 1994, Christie reported that NASDAQ market-makers appeared never to make odd-eighth quotes and wondered if there was collusion between the dealers which facilitated excessive dealing profits at the expense of investors. More recently, Barclay et al. (1999) report on the changes to the NASDAQ market since 1994. The SEC introduced reforms that were effective from January 1997 whereby the public could submit limit orders and compete against the market makers. The Department of Justice investigation required three changes to market practices: (i) the ending of the convention of odd-eighth quotes, (ii) the separation of NASDs' regulatory responsibility from its operational control and (iii) a mandatory display of customer limit orders and the dissemination of prices in proprietary trading systems to impart some auction characteristics to the market. The scandal and investigations resulted in the spreads reported in January 1997 generally being half of those which existing in 1994.

Chung, Van Ness and Van Ness (1999) discuss the difference between (i) conventional order- and quote-driven markets and (ii) markets where there is a 'specialist' who provides liquidity for stocks when there are few limit order trades in the system. The authors found that spreads are widest at the beginning and end of the day, when there are relatively few limit order

[4] Earlier evidence from the Wilson Report (1977) suggested that the direct cost of a placing (2.6%) was lower than for a rights issue (4%).

flows, and that during the middle part of the day spreads narrow considerably. They therefore concluded that limit order trades provide liquidity and immediacy to the market, with the activities of specialists playing an important part in ensuring an order flow throughout the day. These studies seem to suggest that there may significant scope for cost reduction in markets where there is competition and a transparent pricing structure. When companies raise finance through rights issues, placings, open offers and bond issues, there may be very little competition and no price transparency. Therefore considerable scope may exist for cost reduction if the issue processes are documented and the reasons why companies prefer one form of issue from another are investigated; establishing market participants' views about these issues was one of the key motivations for the study.

In this study we report the results of discussions with the fund managers of a leading UK investment trust about the factors which they consider to have an important influence on firms' choice of equity issue method. Our decision to interview fund managers before speaking to equity issuers themselves was made because of the inconclusive nature of large-sample aggregate analyses in establishing the determinants of corporate fund raising behaviour. We chose to investigate this particular aspect of corporate financing activity because recent evidence from firms listed on the London Stock Exchange suggests that the negative market reaction to SEO announcements only occurs when the fund raising takes the form of a rights issue. For example, Armitage (1999) examines 124 SEOs made in the UK between 1985 and 1996 and finds that the two-day average announcement period abnormal return is -3% for rights issues but +1.03% for open offers. Similar results are reported in Burton et al. (2000) who document that the UK market reaction to rights issue announcements is significantly worse than for external placings with financial institutions.[5] These studies indicate that certain types of equity issue do

[5] The 'pre-emptive' right of existing shareholders to participate on a pro-rata basis in any new issue of equity shares has long been a tradition in the UK, as well as forming part of the London Stock Exchange's Listing Rules. Shareholders' rights have also been enshrined in law since 1977 with the legal framework currently being laid out in Sections 89-96 of the 1985 Companies Act; in contrast, placings of shares with external financial institutions were

not adversely affect the share prices of UK firms, but (and contrary to the situation in many other countries including the US[6]) UK companies continue to make extensive use of the rights offer method to raise new equity funds.

Our decision to focus on the choice of equity offer method made by UK firms was further motivated by the fact that early results from large-sample research have not proved successful in identifying the variables which influence corporate behaviour. Burton and Power (2000) compared the financial characteristics of firms making the 193 rights and 329 external placings of equity announced by UK firms in 1995 and 1996 in an attempt to build a predictive model of corporate equity offer method choice. The variables used by the authors to identify differences between rights- and non rights-issuers were all based on conventional finance logic and included firm size, profitability, shareholder structure, prior offering methods and liquidity. Despite the apparent logic behind the choice of the variables, the authors reported that the only significant difference between the two classes of firms is that rights issuers were larger than their placing issuer counterparts. Even this finding is shown not to provide investors with the ability to predict issuing methods accurately.

3. Research Method

The research approach adopted in this study involved a visit to one financial institution in Scotland where two individuals were interviewed. Both interviewees had been with the firm for an average of 15 years and had been promoted to relatively senior positions within the organisation. The two individuals were in charge of equity portfolios with a market value of several billion pounds and had observed many of their actual and potential investee firms issue

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only introduced by the London Stock Exchange in 1975. To undertake a placing, a firm must frst obtain shareholders' permission at a general meeting; however, the 'Pre-emption Group' of major UK institutional shareholders advises its members to vote against placings (in the absence of a clawback to existing shareholders via an 'open offer') if the total amount placed in any twelve-month period is greater than 5% of existing share capital. A rolling three-year limit of 7.5% also currently applies.

shares. They were willing to supply their insights on decisions by firms about whether and how to raise equity as well as highlighting how the SEO process had changed over the last decade both here and in the USA. Most importantly, their familiarity with the SEO process meant that they were able to offer valuable advice about the questions and issues which they believed should form a central part of our subsequent discussions with listed firms that had recently issued equity.

A semi-structured questionnaire was used to guide the discussion for this interview. The questions in this questionnaire were drawn from the SEO literature discussed in Section 2 of the paper. The interview was conducted by two members of the research team, lasted for just under two hours and was recorded on tape; detailed notes were also taken. The tape was transcribed and the comments distilled in the remaining sections of the paper.

4. Results

Three main factors were identified as influencing a company's decision to issue shares. First, both interviewees agreed that cyclical factors have an affect on corporate fund raising activities; equity issues were fashionable in certain periods while debt financing was popular in others. For example, interviewee A commented that:

> "There was a time when everyone in the UK had a rights issue ... and then started moaning when it went wrong. But with the fall in inflation ... the cost of debt has shrunk rapidly and there has been a fashionable return (to the belief) that companies are not geared up enough ... and should issue debt. If we have a turnaround and these companies find themselves financially stretched, we may get a return to corporate finance departments driving equity issues".

While this view concurs broadly with the approach adopted in earlier large sample studies (see, e.g. Choe et al., 1993), the situation appears more complex in practice with macro-economic influences on the relative costs of sources of finance also being important.

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[6] Eckbo and Masulis (1992) note that almost half of all US SEOs took the form of rights issues until the 1960s; the equivalent figure today is less than 1%. In contrast, Burton et al. (2000) report that nearly 40% of equity offers in the

Second, the two financial experts strongly believed that, contrary to the impression which might be gained from large sample studies, company decisions to issue equity were primarily driven by the exhortations of corporate finance departments in merchant banks. They suggested that staff in these departments regularly contacted companies which had not raised funds for a significant length of time in an attempt to generate business for their institutions. Interviewee B pointed out that:

> "There is a large element of fashion (to the decision about an SEO) and a great deal of this is driven by corporate finance departments. (Firms) will have their named corporate financiers and will have discussions with them about raising funds."

Interviewee A agreed that merchant banks were active participants in the market, trying to stimulate business in sectors where competitors were already proceeding with an SEO. However, he indicated that a company's decision to raise funds by issuing shares varied from one firm to another according to the experience and background of the executives in charge:

> "There are companies that listen to their Merchant Banks and there are companies that don't ... (Some companies) have a strong independent capability ... and have a view about what they are doing ... there are others ... with different objectives such as making the firm bigger."

Interviewee A concurred when he noted that:

> "If a company is driven by a sales man, they will listen to the bankers more but if it's driven by ...a finance man, they will be (guided by) the numbers."

The interviewees also pointed to the increasingly important role played by US investment banks and a more general trend to American style issuing practices.

Finally, the interviewees stated that the availability of investment opportunities and the existence of growth prospects were an important determinant in deciding to raise funds. In order to convince institutions to take up the shares, companies had to know what they planned to do

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UK between 1995-1996 took the form of rights issues.

with any share issue proceeds. Senior executives typically held "road shows" where they met potential investors and talked about their firm's need for cash and outlined what they were going to spend cash on.[7] For example, if the issue was undertaken to enable the takeover of a cash rich firm then debt financing was likely since the acquired cashflows would fund the repayment of interest and principal associated with the loans.

The two interviewees also had clear views about the more specific question of why some firms use rights issues while others prefer to place shares with external financial institutions. The size of a company was suggested as having a significant influence on the form of equity issue decided upon. For example, Interviewee A suggested that a placement was likely "if the company were to be able to expand the range of names on its share register in a useful way". He added that a rights issue would not be popular "if a small company was trying to get a wider (group) of people following them and to get its recognition up". Interviewee B commented that from the point of view of an investee institution, a rights issue would be looked upon more favourably if the company was likely to perform well in the future:

> "If its a good company that we like, we would be reluctant to see them go down the private placement route. We have to stand up for our interests."

Another major consideration affecting the choice between a rights issue and a placing was the amount of funds to be raised. The interviewees pointed out that placings tended to be used for smaller issues because most firms are well aware of the rules permitting them to place only a small percentage of capital without first offering the shares to existing equity holders.[8] For example, Interviewee B commented that:

> "In general most companies act for disapplication of pre-emption rules on up 5% of capital; for some new growing aggressive business ... it is very easy to go out....and place several thousand shares (which only add) up to 0.1% of capital. Because of the nature of certain businesses, it is much easier to do multiple little deals issuing capital without having to worry about pre-emption requirements at much less cost."

[7] These briefings usually took place in Edinburgh and London.

The speed with which issues can be undertaken is frequently cited in texts as a major influence on SEO method. Interviewee B agreed with this notion when he argued that:

> "Timing is ... important. The small placings can be completed in a matter of days while larger rights issues can take several months."

Interviewee A suggested that this question of timing was no longer a serious problem in the UK. He pointed out that:

> "Companies very often have the staff on the stocks; they are pretty well teed up to have a rights issue to the appropriate level if the right acquisition comes along ... They will have a lot of the material ready."

The financial health of the equity-issuing firm also had a bearing on whether a rights issue or a placing occurred. Both interviewees indicated that convincing the relatively small number of investors associated with a placing about the future potential of a firm whose current performance was poor might be less difficult:

> "If you are in a weak position, the placing route would be the safer option (to take) because you might be able to convince the bankers that it is not as bad as it seems ... You might be able to give them more .. information."

Finally a number of characteristics of the market and of the company were thought to play a key role in a firm's choice between a rights issue and a placing. Both the current level of the market and current price of a company's shares were thought to exert a "significant" influence on the decision; higher values of both measures usually suggested that a rights issue might take place. Similarly, good recent news about company profits and growth in EPS tilted the probabilities in favour of a rights issue while, in contrast, a change in company adviser was not thought to be a significant factor as long as the new advisers "were of equivalent quality." The interviewees suggested that a high dividend payout firm was likely to prefer placings, other

[8] The offer is typically made in the form of a 'clawback' via an open offer.

things being equal, because dividends per share (DPS) are often maintained at the pre-rights level.[9] As interviewee B pointed out:

> "The dividend comes into play in the UK traditionally when (a firm) has ... held the dividend while the rights issue has been done at a discount. This has made (rights issues) expensive in terms of the cost of capital."

The unwillingness to adjust DPS after a discounted rights issue was traditionally thought to be caused by concerns about maintaining a high payout and tax considerations in the UK. Interviewee A agreed that:

> "The tax structure in the USA has driven (dividends lower) over the last decade or two while the tax structure in the UK undoubtedly was biased the other way."

However, both agreed that the recent abolition of Advanced Corporation Tax (ACT) might change this situation.

5. Discussion and Implications

The main aim of this interview was to improve and inform our future discussions with a sample of firms which have recently undertaken an SEO; these discussions will attempt to establish why firms issue equity and in particular why they favour certain offer methods. We hoped that by interviewing fund managers prior to speaking with issuing companies we would gain a better understanding of (i) the aspects of current theoretical explanations about why firms issue shares that are worth pursuing and (ii) whether any factors not suggested by conventional textbook analyses are likely to be of practical importance and therefore worth discussing with recent issuers of shares.

[9] The greater discount associated with most rights issues in the UK (typically 15%) compared to placings (typically 5%) means that more shares must be issued under the rights method to raise a given sum. The associated difference

The interview with the fund managers appeared to highlight four issues of direct relevance for our later discussions with companies and for investigations of corporate fund raising activities in general. First, arguably the most important insight gained from the interview related to the important proactive role played by merchant banks and other external advisers, in terms of both the decision to raise new equity financing and the method used to issue the shares. Conventional large sample analyses of corporate fund raising behaviour are based on the implicit assumption that fund raising behaviour, including the choice of share issue method, is internally motivated; the assumption made is that firms examine their own situation before deciding on a course of action and only then bring in financial experts to enable them to proceed with the new financing process. If financial institutions have a significant impact on corporate fund raising behaviour in practice, as our interviewees suggested, it becomes difficult for researchers to observe and incorporate all the key influences on firms' financing activities, to the extent that conventional aggregate analysis may simply not be appropriate when attempting to model companies' decision making in the area.

Second, even when important variables are observable by researchers, their influence may vary dramatically from firm-to-firm, again suggesting that case-study research is the most suitable method for investigations into the security issuing behaviour of firms. For example, the interviewees pointed out that different institutions attach varying degrees of importance to pre-emption rights; this indicates that empirical studies of equity issue method choice, such as Burton and Power (2000), are right to attempt to incorporate shareholder structure variables in their models. However, the role of such variables in practice is more subtle, depending on the attitudes of a company's institutional investors, and on how well these views are known to firms. The role of merchant banks was also thought to vary from firm-to-firm with the background of senior directors likely to affect a firm's response to external financial advice. The potential for

in potential dilution of earnings per share figures is a possible explanation for the rights offer paradox discussed earlier.

the influence of certain variables to vary across companies has therefore had a significant impact on the nature of our discussions with individual issuing companies.

Third, it was clear from the interview that even when a variable is observable, and its effect generalisable across firms, the nature of the influence may be more complex than prior empirical studies have assumed. The best example of this complexity related to the influence of cyclical factors on the decision to issue equity; the interviewees agreed that these matters were important, but suggested that in practice their role was bound up with variability in other macro-economic indicators, particularly inflation and its effect on the relative costs of different sources of financing. Also, the interviewees argued that in reality placings can be arranged more quickly than rights issues, but only for issues falling below the 5% pre-emption threshold; no timing benefit was believed to exist for larger issues where the specific approval of shareholders would be required. These insights will allow us to examine how the influence of particular variables is bound up with other factors when asking firms about the role of specific financial data in affecting their fund raising behaviour.

Finally, the interviews highlighted that certain factors have an impact on corporate decisions about external fund raising in a relatively straight forward way, suggesting that we should ensure they from part of our discussions with issuing firms. For example, the interviewees noted that concerns about earnings per share dilution might lead firms to avoid rights issues when profits are low and falling; this evidence is in line with hypotheses contained in Burton and Power (2000). The interview also supported Burton and Power's prediction of a positive relationship between issue size and the propensity to favour rights over placing issues, but the reasons suggested by the interviewees are rather different from the agency- theory based explanation put forward in the earlier investigation. The results of the interview also suggest, however, that one of the variables used in prior studies of the rights/ placing choice may influence firms in precisely the opposite way to that proposed in earlier studies. In particular, the interviewees believed that high dividend firms are more likely to use placings because of concerns about the diluting effect of heavily discounted rights issues and the need to maintain post-issue dividend per share levels. In Burton and Power (2000) the authors assumed that the effect of a high payout ratio in reducing asymmetry of information dominated any other role for dividend data, with placings therefore being more likely in the presence of significant agency problems and attendant difficulties in persuading existing shareholders to increase their investment in the firm.

6. Conclusions

This study reports the results of a detailed interview with experienced fund managers, the findings of which will form the basis for a series of interviews with equity-issuing firms that are currently being conducted. We believed that undertaking such an interview prior to speaking to individual companies would be important in helping us to focus on the issues that are relevant to firms in practice and we believe that our findings bear this out. It was felt that undertaking such a study was particularly important given the inconclusive nature of the many large-sample empirical studies which dominate (i) investigations of corporate debt-equity choices and (ii) decisions about equity issue methods. Our results suggest that some of the variables which influence firms' fund raising behaviour in practice are simply not observable to researchers, unless they speak to firms directly and solicit their views about their the attitudes of their shareholders and other matters. The discussion with the fund managers also indicates that the impact of certain key variables varies across firms. These and the other findings discussed above have implications both for our interviews with equity issuers which are now underway, and for any researcher undertaking and/or interpreting empirical studies of corporate behaviour on the basis that firms are relatively homogeneous in terms of how and why they raise external capital.

Of course there are a number of limitations to the analysis of this paper. First, it is preliminary in that it sets the scene for a more extensive investigation which is currently underway. Second, it is based on only one interview with two Scottish fund managers; the views of the two interviewees may not be commonly held (i) by other fund managers in Scotland and (ii) by others who work in different areas of the financial sector throughout the UK. Third, a semi-structured questionnaire was employed where the questions emerged from the literature which we are trying to verify. This apparent circularity was overcome, to an extent, by enabling the interviewees (a) to raise issues which we had not considered and (b) to highlight topics which we had not asked about but which they thought relevant. Overall, we believe that the results of the paper are potentially useful in helping researchers ask the right questions when examining voluntary corporate decision making.

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