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International Evidence on Financial Derivatives Usage

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Abstract

Theory predicts that nonfinancial corporations might use derivatives to lower financial distress costs, coordinate cash flows with investment, or resolve agency conflicts between managers and owners. Using a new database, we find that traditional tests of these theories have little power to explain the determinants of corporate derivatives usage. Instead, we show that derivative usage is determined endogenously with other financial and operating decisions in ways that are intuitive but not related to specific theories for why firms hedge. For example, derivative usage helps determine the level and maturity of debt, dividend policy, holdings of liquid assets, and international operating hedging.

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