

## [There's a very strange American idea about dividends](#) [1]

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I'm always confused by a slightly strange American idea about dividends. That if they are paid they are somehow wasted. This from Matt Yglesias is only one expression of the idea, there are [many others](#) [2]:

Dividends, by contrast, have a weak and indirect impact on the economy and don't really serve anyone's long-term interests. We're left hoping that rich shareholders will spontaneously develop enough appetite for extra yachts to push the economy forward. It's a broken economic model that only deepens the disconnect between the stock market recovery and the ongoing labor market slump.

This is entirely wrong, of course. Dividends are the returning to shareholders of some portion of the company's profits. OK, that much is fine: but what happens then?

Well, two things need to be kept in mind. The first is that pretty much all innovation and again, pretty much all of jobs growth comes from new firms. Extant firms tend to reduce their number of employees over time as they become more efficient at whatever it is that they do. So, we'd really rather like some method of getting money out of extant companies and into new ones.

The second is that most stocks and shares are held either by wealthy people or by the various pension and insurance funds. And what is it that we know about those two groups? Any dividend income that they receive is likely to be reinvested. And that will of course be into different companies than the ones they received the dividends from and some portion of it will indeed flow to new companies.

Hurrah! we now have our method of directing the profits from extant companies into the financing of new ones which is the very thing that we desire in order for there to be further innovation and growth in the economy.

Dividends are not some short term failing of the financial marketplace, they're the very basis of its long term success.

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