10th International Paris Finance Meeting

December 20, 2012

Novotel Paris les Halles Hotel
Place Marguerite de Navarre
75001 PARIS

www.eurofidai.org/december2012.html

INSTITUT CDC
POUR LA RECHERCHE

Meeting's organization

Since 1979, the French Finance Association (AFFI) has brought together researchers, teachers and practitioners interested in financial management.

Its objective is to develop communication between members thus contributing to enhanced progress in the financial management discipline.

AFFI sets up meetings, publishes a specialized review (Finance) and supports financial research (AFFI-Financial Markets price, AFFI-FNEGE price...).

More information:
www.affi.asso.fr

Eurofidai (European Financial Data Institute) is an academic institute funded by the French National Center for Scientific Research (CNRS).

Its mission is to **develop European stock exchange databases that are useful to finance academic researchers.** That's why Eurofidai works in creating **verified, controlled and homogeneous databases over long periods.**

Through its website, Eurofidai provides access to stock exchange databases for European as well as Asia and Middle East countries : stock daily data, indexes, intraday data, mutual funds, corporate actions...

More information:
www.eurofidai.org

Numbers

272 papers were submitted for presentation at the meeting. Of this number, only 48 were accepted indicating rigorous selection criteria.

In 2012, submissions were received from the United States (56), France (49), Germany (38), the United Kingdom (18), Switzerland (14), Canada (13), the Netherlands (12), Italy (10), Australia (9), Denmark (7), Greece (5), Norway (5), Singapore (5), Spain (5), Belgium (4), China (3), other European countries (7) and 12 from the rest of the world.

Based on presenter's affiliation, the 48 accepted articles came from the United States (9), France (8), Germany (7), Canada (4), the United Kingdom (4), the Netherlands (3), Italy (2), Norway (2), Belgium (2), Sweden (2), Denmark (1), Luxembourg (1), Spain (1), Switzerland (1) and Russia (1).

Compared with the previous editions of the meeting, there is an increasingly large and strong body of quality work coming from

Program chair

Patrice Fontaine (EUROFIDAI, CNRS & University of Grenoble 2)

2012 Scientific Committee

Sessions were organized by :

Aït-Sahalia Yacine (Princeton University and NBER)
Aktas Nihat (Univ. Lille Nord de France - SKEMA)
Alexandre Hervé (Paris Dauphine University)
Broihanne Marie Hélène (University of Strasbourg)
Degeorge François (University of Lugano)
Derrien François (HEC Paris)
Dumas Bernard (INSEAD)
Fontaine Patrice (Eurofidai and University of Grenoble 2)
Hege Ulrich (HEC Paris)
Le Courtois Olivier (EM Lyon Business School)
Lioui Abraham (EDHEC)
Moinas Sophie (University of Toulouse 1)
Moraux Franck (University of Rennes 1)
Petey Joël (University of Strasbourg)
Pouget Sébastien (University of Toulouse 1)
Quittard-Pinon François (EM Lyon Business School)
Refait-Alexandre Catherine (University of Franche-Comté)
Sentis Patrick (University of Montpellier 1)
Viviani Jean Laurent (University of Rennes 1)

Program

08h30 Registrations

09h00 Asset Pricing

09h00 Behavioral Finance

09h00 Corporate Governance

09h00 Financial Crisis

10h30 **Coffee Break**

11h00 CEO and Governance

11h00 Microstructure

11h00 Financial Intermediation

11h00 Portfolio Management

11h00 Eurofidai financial databases presentation

12h45 **Lunch**

14h15 Hedge-Mutual Funds

14h15 International Finance

14h15 Interest Rates

14h15 Private Equity and Venture Capital

15h45 **Coffee Break**

16h15 Derivatives

16h15 Financial Markets

16h15 Financial Econometrics

16h15 Mergers and Acquisitions

16h15 Eurofidai financial databases presentation

18h00 **Cocktail**

09h00 Asset Pricing

Chairman: Lioui A. (EDHEC)

HIGH ORDER SMOOTH AMBIGUITY PREFERENCES AND ASSET PRICES
Thimme Julian (University of Muenster); Völkert Clemens (University of Muenster)
Discussant: Tedongap Romeo (Stockholm School of Economics)

FREQUENCY OF CONSUMPTION ADJUSTMENT AND THE EQUITY PREMIUM
Bulusu Narayan (Bank of Canada); Gomez Biscarri Javier (Universitat Pompeu Fabra)
Discussant: Ghosh Anisha (Tepper School of Business, Carnegie Mellon University)

HABIT FORMATION HETEROGENEITY: IMPLICATIONS FOR AGGREGATE ASSET PRICING
Dubin Eduard (Goethe University); Grishchenko Olesya V. (Federal Reserve Board); Kartashov Vasily (Goethe University)
Discussant: Dumas Bernard (INSEAD)

09h00 Behavioral Finance

Chairman: Pouget S. (University of Toulouse 1)

LEARNING TO CHOOSE THE RIGHT INVESTMENT IN AN UNSTABLE WORLD
Payzan-LeNestour Elise (Australian School of Business); Bossaerts Peter L. (California Institute of Technology)
Discussant: Célérier Claire (University of Zürich)

DOES ACADEMIC RESEARCH DESTROY STOCK RETURN PREDICTABILITY?
McLean R. David (University of Alberta); Pontiff Jeffrey (Boston College)
Discussant: Payzan-LeNestour Elise (Australian School of Business)

WHAT DRIVES FINANCIAL COMPLEXITY? A LOOK INTO THE EUROPEAN RETAIL STRUCTURED PRODUCTS MARKET
Célérier Claire (University of Zürich); Vallée Boris (HEC Paris)
Discussant: McLean R. David (University of Alberta)

09h00 Corporate Governance

Chairman: Derrien F. (HEC Paris)

CAPITAL STRUCTURE AND EMPLOYMENT FLEXIBILITY
Kuzmina Olga (New Economic School)
Discussant: Irina Ivashkovskaya (National Research University, Russia)

PRODUCTION CHARACTERISTICS, REAL FLEXIBILITY, AND THE CAPITAL STRUCTURE DECISIONS
Reinartz Sebastian J. (Technische Universität München); Schmid Thomas (Technische Universität München)
Discussant: Kuzmina Olga (New Economic School)

WHICH TYPES OF FIRMS REACT MORE TO A TAX CUT? EVIDENCE FROM THE 2003 DIVIDEND TAX CUT
Lai Tat-kei (Copenhagen Business School); Ng Travis (The Chinese University of Hong Kong)
Discussant: Schmid Thomas (Technische Universität München)

09h00 Financial Crisis

Chairman: Hege U. (HEC Paris)

TRANSPARENCY IN THE FINANCIAL SYSTEM: ROLLOVER RISK AND CRISES
Bouvard Matthieu (McGill University) ; Chaigneau Pierre (HEC Montreal) ; De Motta Adolfo (McGill University)
Discussant: Stebunovs Viktors (Federal Reserve Board)

CIRCUIT BREAKERS AND MARKET RUNS
Draus Sarah (University of Naples Federico II); Van Achter Mark (Erasmus University)
Discussant: Chaigneau Pierre (HEC Montreal)

FIRM AND HOUSEHOLD ACCESS TO CREDIT AND NON-FINANCIAL EMPLOYMENT OVER THE GREAT RECESSION
Haltenhof Samuel (Federal Reserve Board); Lee Seung Jung (Federal Reserve Board); Stebunovs Viktors (Federal Reserve Board)
Discussant: Banti Chiara (City University of London)

11h00 CEO and Governance

Chairman: Alexandre H. (Paris Dauphine University)

ORDERS OF MERIT AND CEO COMPENSATION: EVIDENCE FROM A NATURAL EXPERIMENT
Siming Linus (Bocconi University)
Discussant: Zhivotova Evgenia (University of Mannheim)

THE CORPORATE GOVERNANCE ENDGAME - AN ECONOMIC ANALYSIS OF MINORITY SQUEEZE - OUT REGULATION IN GERMANY
Croci Ettore (Universita' Cattolica del Sacro Cuore); Ehrhardt Olaf (University of Applied Sciences Stralsund); Nowak Eric (University of Lugano)
Discussant: Siming Linus (Bocconi University)

PRIDE AND PRESTIGE: WHY SOME FIRMS PAY THEIR CEOs LESS
Maug Ernst (University of Mannheim); Niessen-Ruenzi Alexandra (University of Mannheim); Zhivotova Evgenia (University of Mannheim)
Discussant: Zhao Shan (Grenoble School of Management)

11h00 Financial Intermediation

Chairman: Refait-Alexandre C. (University of Franche-Comté)

BANK RISK EXPOSURE, BANK FAILURE AND OFF BALANCE SHEET ACTIVITIES: AN EMPIRICAL ANALYSIS FOR U.S. COMMERCIAL BANKS
Ziadeh Noma (University of Limoges)
Discussant: Jabbour Ravel (Imperial College Business School)

MORTGAGE SECURITIZATION: THE GOOD, THE BAD, OR THE IRRELEVANT?
Dong Gang Nathan (Columbia University)
Discussant: Ziadeh Noma (University of Limoges)

THE IMPACT OF REGULATORY RISK-BASED CAPITAL REQUIREMENTS ON CREDIT CRISES
Cathcart Lara (Imperial College Business School); El-Jahel Lina (Imperial College Business School); Jabbour Ravel (Imperial College Business School)
Discussant: Dong Gang Nathan (Columbia University)

11h00 Microstructure

Chairman: Moinas S. (University of Toulouse 1)

PUBLIC NEWS ARRIVAL AND CROSS-ASSET CORRELATION BREAKDOWN:IMPLICATIONS FOR ALGORITHMIC TRADING
Ho Kin-Yip (Australian National University); Liu Wai-Man (Australian National University);Yu Jing (University of Western Australia)
Discussant: Bart Zhou Yueshen (VU University Amsterdam)

BELIEF-FREE PRICE FORMATION
Horner Johannes (Yale University); Lovo Stefano (HEC Paris); Tomala Tristan (HEC Paris)
Discussant: Ho Kin-Yip (Australian National University)

MIDDLEMEN INTERACTION AND ITS EFFECT ON MARKET QUALITY
Menkveld Albert J. (VU University Amsterdam); Bart Zhou Yueshen (VU University Amsterdam)
Discussant: Lovo Stefano (HEC Paris)

11h00 Portfolio Management

Chairman: Fontaine P. (University of Grenoble 2 - CNRS)

AN ANATOMY OF FUNDAMENTAL INDEXING
De Moor Lieven (Hogeschool-Universiteit Brussel); Liu Fang (Central University of Finance and Economics, Beijing); Sercu Piet M. F. A. (FEB at KU Leuven); Vinaimont Tom (City University of Hong Kong)
Discussant: Vestman Roine (Stockholm University and SIFR)

DO FUND INVESTORS KNOW THAT RISK IS SOMETIMES NOT PRICED?
Irek Fabian (University of Luxembourg); Lehnert Thorsten (University of Luxembourg)
Discussant: Sercu Piet M. F. A. (FEB at KU Leuven)

LIMITED STOCK MARKET PARTICIPATION AMONG RENTERS AND HOME OWNERS
Vestman Roine (Stockholm University and SIFR)
Discussant: Michala Dimitra (University of Luxembourg)

11h00 Eurofidai financial databases presentation

14h15 Hedge-Mutual Funds

Chairman: Broihanne M.H. (University of Strasbourg)

MONEY FOR NOTHING? UNDERSTANDING VARIATION IN REPORTED HEDGE FUND FEES
Ramadorai Tarun (University of Oxford); Streatfield Michael (University of Oxford)
Discussant: Lambert Marie (University of Liège and Maastricht University)

MOMENTUM STRATEGIES IN FUTURES MARKETS AND TREND-FOLLOWING FUNDS
Baltas Akindynos-Nikolaos (Imperial College Business School); Kosowski Robert (Imperial College Business School)
Discussant: Streatfield Michael (University of Oxford)

HIGHER-MOMENT RISK EXPOSURES IN HEDGE FUNDS
Hubner Georges (HEC Management School, University of Liège); Lambert Marie (University of Liège and Maastricht University); Papageorgiou Nicolas A. (HEC Montreal)
Discussant: Baltas Akindynos-Nikolaos (Imperial College Business School)

14h15 Interest Rates

Chairman: Quittard-Pinon F. (EM Lyon Business School)

A MODEL OF THE EURO-AREA YIELD CURVE WITH DISCRETE POLICY RATES
Renne Jean-Paul (Banque de France)
Discussant: Rostek Stefan (University of Tuebingen)

ON THE OPTIMAL TYPE AND LEVEL OF GUARANTEES FOR PROSPECT THEORY INVESTORS
Ebert Sebastian (University of Bonn); Koos Birgit (University of Bonn); Schneider Judith C. (University of Muenster)
Discussant: Renne Jean-Paul (Banque de France)

A FRACTAL VERSION OF THE HULL-WHITE INTEREST RATE MODEL
Hainaut Donatien (ESC Rennes School of Business)
Discussant: Schneider Judith C. (University of Muenster)

14h15 International Finance

Chairman: Dumas B. (INSEAD)

FINANCIAL GLOBALIZATION AND RISK SHARING: WELFARE EFFECTS AND THE OPTIMALITY OF OPEN MARKETS
Trzcinka Charles A. (Indiana University); Ukhov Andrey D. (Indiana University)
Discussant: Van Achter Mark (Erasmus University)

FEEDBACK TRADING AND INTERNATIONAL PORTFOLIO ALLOCATION
Kinnunen Jyri (Lappeenranta University of Technology)
Discussant: Ukhov Andrey D. (Indiana University)

FX MARKET ILLIQUIDITY AND FUNDING LIQUIDITY CONSTRAINTS
Banti Chiara (City University London); Phylaktis Kate (City University London)
Discussant: Kinnunen Jyri (Lappeenranta University of Technology)

14h15 Private Equity and Venture Capital

Chairman: Sentis P. (University of Montpellier 1)

CURRYING FAVOR WITH TOP VENTURE CAPITAL FIRMS: THE ROLE OF IPO UNDERPRICING AND ALL-STAR COVERAGE
Bradley Daniel J. (University of South Florida); Kim Incheol (University of South Florida); Krigman Laurie (Babson College)
Discussant: Moeller Thomas (Texas Christian University)

INVESTOR HORIZON AND INNOVATION: EVIDENCE FROM PRIVATE EQUITY FUNDS
Barrot Jean-Noel (HEC Paris)
Discussant: Krigman Laurie (Babson College)

PRIVATE EQUITY FUNDRAISING, FUND PERFORMANCE AND FIRM SPECIALIZATION
Gejadze Maia (Université catholique de Louvain); Giot Pierre (University of Namur); Schwienbacher Armin (Univ. Lille Nord de France - SKEMA)
Discussant: Barrot Jean-Noel (HEC Paris)

16h15 Derivatives

Chairman: Le Courtois O. (EM Lyon Business School)

EXPLAINING THE VOLATILITY SURFACE: A CLOSED-FORM SOLUTION TO OPTION PRICING IN A FRACTIONAL JUMP-DIFFUSION MARKET
Rostek Stefan (University of Tuebingen)
Discussant: Lévy-Véhel Jacques (INRIA)

THE FINE STRUCTURE OF VARIANCE: CONSISTENT PRICING OF VIX DERIVATIVES
Branger Nicole (University of Muenster); Völkert Clemens (University of Muenster)
Discussant: Donatien Hainaut (ESC Rennes Business School)

DETECTION OF ARBITRAGE IN A MARKET WITH MULTI-ASSET DERIVATIVES AND KNOWN RISK-NEUTRAL MARGINALS
Tavin Bertrand (Université Paris 1 - Panthéon Sorbonne)
Discussant: Bernard Carole (Waterloo University)

16h15 Financial Econometrics

Chairman: Aït-Sahalia Y. (Princeton University)

CAN INTERNET SEARCH QUERIES HELP TO PREDICT STOCK MARKET VOLATILITY?
Dimpfl Thomas (University of Tuebingen); Jank Stephan (Frankfurt School of Finance & Management)
Discussant : Holcblat Benjamin (Norwegian Business School, BI Oslo)

A STRUCTURAL MODEL OF DYNAMIC MARKET TIMING: THEORY AND ESTIMATION
Detemple Jérôme (Boston University); Rindisbacher Marcel (Boston University)
Discussant : Jank Stephan (Frankfurt School of Finance & Management)

A CLASSICAL MOMENT-BASED APPROACH WITH BAYESIAN PROPERTIES: ECONOMETRIC THEORY AND EMPIRICAL EVIDENCE FROM ASSET PRICING
Holcblat Benjamin (Norwegian Business School, BI Oslo)
Discussant : Detemple Jérôme (Boston University)

16h15 Financial Markets

Chairman: Viviani J.L. (University of Rennes 1)

THE VALUE PREMIUM IN A LARGE-CROSS SECTION OF TEST PORTFOLIOS
Barras Laurent (McGill University)
Discussant: Cujean Julien (Swiss Finance Institute)

LEISURE, CONSUMPTION AND LONG RUN RISK: AN EMPIRICAL EVALUATION
Zhang Xiang (Autonomous University of Barcelona)
Discussant: Barras Laurent (McGill University)

THE SOCIAL DYNAMICS OF PERFORMANCE
Cujean Julien (Swiss Finance Institute)
Discussant: Zhang Xiang (Autonomous University of Barcelona)

16h15 Mergers and Acquisitions

Chairman: Aktas N. (Univ. Lille Nord de France - SKEMA)

TARGET FINANCIAL INDEPENDENCE, BARGAINING POWER, AND TAKEOVER PRICING
Jindra Jan (Ohio State University); Moeller Thomas (Texas Christian University)
Discussant: De Bodt Eric (Univ. Lille Nord de France - SKEMA)

BID RESISTANCE BY TAKEOVER TARGETS: MANAGERIAL BARGAINING OR BAD FAITH?
Bates Thomas W. (Arizona State University); Becher David A. (Drexel University)
Discussant: Schwienbacher Armin (Univ. Lille Nord de France - SKEMA)

WHAT DRIVES THE VARIATION IN TAKEOVER CONTRACTS: THE ECONOMICS OR THE LAWYERS?
Karsten Christel (University of Amsterdam)
Discussant: Bollaert Helen (Univ. Lille Nord de France - SKEMA)

16h15 Eurofidai financial databases presentation

09h00 Asset Pricing

Chairman: Lioui A. (EDHEC)

HIGH ORDER SMOOTH AMBIGUITY PREFERENCES AND ASSET PRICES

Thimme Julian (University of Muenster) - julian.thimme@wiwi.uni-muenster.de ; Völkert Clemens (University of Muenster)

Discussant: Tedongap Romeo (Stockholm School of Economics)

This paper extends the recursive smooth ambiguity decision model developed in Klibanoff, Marinacci, and Mukerji (2005, 2009) by relaxing the uniformity imposed on higher order acts. This generalization permits a separation of intertemporal substitution, risk aversion, and ambiguity aversion towards different sources of uncertainty. Our decision model is suited in situations where subjects may treat several kinds of uncertainty in different manners. We apply our preference specification to a consumption-based asset pricing model with long-run risks and assess the impact of ambiguity on asset prices and predictability patterns. We find that modeling attitudes towards uncertainty through high order smooth ambiguity preferences has important implications for asset prices. Our model significantly improves upon the special cases of Epstein and Zin (1989) utility and standard smooth ambiguity preferences.

FREQUENCY OF CONSUMPTION ADJUSTMENT AND THE EQUITY PREMIUM

Bulusu Narayan (Bank of Canada) - narayan.bs@gmail.com ; Gomez Biscarri Javier (Universitat Pompeu Fabra)

Discussant: Ghosh Anisha (Tepper School of Business, Carnegie Mellon University)

We show that two types of consumption risk are priced in the equity premium: the risk of aggregate consumption growth and that of changing the composition of the consumption basket, when goods have heterogeneous costs of adjustment. We use the property that the frequency of consumption adjustment is inversely related to adjustment costs and split consumption into two components that proxy for consumption of low and high adjustment cost goods. We then estimate a version of the CCAPM with two components of consumption and show that our proposed split helps resolve the equity premium puzzle, while simultaneously generating sufficient volatility of marginal utility to satisfy volatility bounds at all frequencies.

HABIT FORMATION HETEROGENEITY: IMPLICATIONS FOR AGGREGATE ASSET PRICING

Dubin Eduard (Goethe University); Grishchenko Olesya V. (Federal Reserve Board) - olesya.v.grishchenko@frb.gov; Kartashov Vasily (Goethe University)

Discussant: Dumas Bernard (INSEAD)

We explicitly solve for the aggregate asset pricing quantities of a general equilibrium Lucas endowment economy inhabited by two agents with habit formation preferences. Preferences are modeled either as internal or external habits. We allow for agents' heterogeneity in relative risk aversion and habit strength. Equilibrium quantities, such as equity premium, equity volatility, Sharpe ratio, interest rate volatility, and asset holdings are computed using a recently developed algorithm of Dumas and Lyasoff (2011). The algorithm is refined to capture time-nonseparability induced by habit. We obtain that internal habits provide for a considerable improvement in obtaining aggregate asset pricing quantities consistent with historically observed magnitudes as opposed to catching up with Joneses» preferences.

Behavioral Finance

Chairman: Pouget S. (University of Toulouse 1)

LEARNING TO CHOOSE THE RIGHT INVESTMENT IN AN UNSTABLE WORLD

Payzan-LeNestour Elise (Australian School of Business) - elise@unsw.edu.au ; Bossaerts Peter L. (California Institute of Technology)

Discussant: Célérier Claire (University of Zürich)

Many argue that complexity is a decisive obstacle to sophisticated learning, especially in financial markets. Here we simulate reward structures in financial markets with a multi-armed restless bandit. The reward probabilities of the arms change abruptly («jump») over the experimental session. We contrast Bayesian learning with reinforcement learning, an intuitive and straightforward approach, which has become the workhorse of learning theory in behavioral sciences. Despite high computational demands in the task, we find substantial evidence in favor of Bayesian updating. We discuss how «nudging» agents into paying attention to the right things, and offering high monetary incentives, may be pivotal for the emergence of sophisticated behavior.

DOES ACADEMIC RESEARCH DESTROY STOCK RETURN PREDICTABILITY?

McLean R. David (University of Alberta) - rdmclean@ualberta.ca ; Pontiff Jeffrey (Boston College)

Discussant: Payzan-LeNestour Elise (Australian School of Business)

We study the out-of-sample and post-publication return-predictability of 56 characteristics identified in the academic literature as predictors of cross-sectional stock returns. The average out-of-sample decay in return-predictability due to statistical bias to be 15%, but not statistically different from zero. The average post-publication decay, caused by both statistical bias and price pressure from aware investors, is about 50%, and statistically different from both 0% and 100%. These results are not explained by time trends in anomaly returns or measures of attention from the academic literature. Consistent with academic research drawing the attention of informed traders, after an anomaly is published it experiences higher correlations with other anomalies that have been published.

WHAT DRIVES FINANCIAL COMPLEXITY? A LOOK INTO THE EUROPEAN RETAIL STRUCTURED PRODUCTS MARKET

Célérier Claire (University of Zürich) - claire.celerier@gmail.com ; Vallée Boris (HEC Paris)

Discussant: McLean R. David (University of Alberta)

This paper investigates the relationship between complexity and competition in household finance. We theoretically show how banks with heterogeneous market shares can use complexity to capture an informational rent from unsophisticated investors. This generates a U-shaped impact of competition on complexity. Using an academically unexploited database of all European issuances of retail structured products since inception, we provide empirical evidence for this prediction. When regressing complexity on competition, we observe a non-monotonous relationship. A cross-sectional regression on distributors' market powers shows that larger competitors offer more complex products. We also find that institutions targeting mainly unsophisticated consumers offer more complex products. These findings add to our understanding of the growing gap between financial complexity and investor sophistication, and how banks can strategically exploit it to their advantage.

09h00

Corporate Governance

Chairman: Derrien F. (HEC Paris)

CAPITAL STRUCTURE AND EMPLOYMENT FLEXIBILITY

Kuzmina Olga (New Economic School) - okuzmina@nes.ru

Discussant: Irina Ivashkovskaya (National Research University, Russia)

This paper uses a unique panel dataset to establish a causal relationship between the use of flexible contractual arrangements with labor and capital structure of the firm. Using the exogenous inter-temporal and cross-regional variation in government labor policies, I find that hiring more temporary workers leads firms to have more debt. Characterized by much lower firing costs, temporary employment contracts allow firms to adjust the labor force and profits upon negative shocks realizations and reduce the default risk on the margin, thereby promoting debt financing. I find the supporting evidence of this mechanism and also interpret it as a substitution between operating and financial leverage. Given the overwhelming extent of labor reforms in continental Europe in recent years that touch upon the incentives to use different employment contracts and are aimed at offering more job security to workers, it is important to understand how such policies would affect firms.

PRODUCTION CHARACTERISTICS, REAL FLEXIBILITY, AND THE CAPITAL STRUCTURE DECISIONS

Reinartz Sebastian J. (Technische Universität München); Schmid Thomas (Technische Universität München) - thomas.schmid@cefs.de

Discussant: Kuzmina Olga (New Economic School)

We analyze the impact of production characteristics on capital structure using a sample of worldwide energy utilities. Detailed information on more than 30,000 single power plants enables us to construct different measures for their production flexibility. We find a positive relationship between production flexibility and leverage. Past regulatory changes in the electricity sector allow us to demonstrate causality. Furthermore, analyzing capital market reactions after the collapse of Lehman Brothers and the coordinated action of international central banks on November 30th, 2011 yields evidence for a substitution effect between production flexibility and financial flexibility.

WHICH TYPES OF FIRMS REACT MORE TO A TAX CUT? EVIDENCE FROM THE 2003 DIVIDEND TAX CUT

Lai Tat-kei (Copenhagen Business School) - tl.eco@cbs.dk ; Ng Travis (The Chinese University of Hong Kong)

Discussant: Schmid Thomas (Technische Universität München)

The agency model of Chetty and Saez (2010) predicts that firms with stronger corporate governance are more responsive to a dividend tax cut in their dividend and investment policies. We test these predictions by exploiting the sudden and significant dividend tax cut following the Jobs and Growth Tax Relief Reconciliation Act of 2003 and the pre-tax cut variation in corporate governance standards across firms. We find that firms with stronger corporate governance raise dividends and reduce investment in response to the tax cut significantly more than firms with weaker corporate governance. These differential reactions come from differences in corporate governance standards but not differences in ownership concentration ratios.

Financial Crisis

Chairman: Hege U. (HEC Paris)

TRANSPARENCY IN THE FINANCIAL SYSTEM: ROLLOVER RISK AND CRISES

Bouvard Matthieu (McGill University) ; Chaigneau Pierre (HEC Montreal) - pierre.chaigneau@hec.ca ; De Motta Adolfo (McGill University)

Discussant: Stebunovs Viktors (Federal Reserve Board)

The paper presents a theory of optimal transparency when financial institutions are exposed to rollover risk. Transparency enhances the stability of the financial system during crises but has destabilizing effects in normal economic times. Thus, the regulator optimally increases transparency during crises. Under this policy, however, increasing transparency signals a deterioration of economic fundamentals, which gives regulators ex-post incentives to withhold information. The theory relates optimal transparency to financial institutions' incentives to diversify their risk and hold liquidity. In particular, the optimal policy reduces the net benefit of diversification and generates an equilibrium level of liquidity that is inefficiently low.

CIRCUIT BREAKERS AND MARKET RUNS

Draus Sarah (University of Naples Federico II); Van Achter Mark (Erasmus University) - mvanachter@rsm.nl

Discussant: Chaigneau Pierre (HEC Montreal)

This paper analyzes whether the application of a «circuit breaker» to a financial market (i.e. a mechanism that interrupts trading for a predetermined period when the price moves beyond a predetermined level) reaches its intended goals of increased market stability and overall welfare. Our framework of analysis is a model in which investors can trade at several dates and might face a liquidity shock forcing them to sell immediately when the shock occurs. This setting potentially induces a «market run» where investors commonly sell merely out of fear other investors are selling and not because they have current liquidity needs. We show that the introduction of a sufficiently tightly-set circuit breaker within this setting successfully prevents this market run from occurring. Even more so, it could induce the socially optimal state (in which trading only takes place when it is motivated by liquidity needs) to arise. However, this desirable equilibrium can only be reached under particular economic conditions. When these conditions are not met, installing a circuit breaker might even lower social welfare as compared to a setting without a circuit breaker as it impedes socially desirable trades and stimulates socially undesirable trades.

FIRM AND HOUSEHOLD ACCESS TO CREDIT AND NON-FINANCIAL EMPLOYMENT OVER THE GREAT RECESSION

Haltenhof Samuel (Federal Reserve Board); Lee Seung Jung (Federal Reserve Board); Stebunovs Viktors (Federal Reserve Board) - stebunov@bc.edu

Discussant: Banti Chiara (City University of London)

We examine how firm and household access to credit affects manufacturing employment. To minimize endogeneity concerns, (a) we exploit variation in employment across industries at the U.S. state level over time and variation in commercial and consumer lending standards, as well as home equity access, at the national level over time; (b) we rely on differences in the degree of external finance dependence and asset tangibility across industries and in the sensitivity of these industries' output to changes in consumer credit. We show that access of households to loans matters more for employment than that of firms and that it affects employment mostly through changes in the average firm size. Per our results, over the Great Recession, for selected industries, tightening access to commercial and consumer loans explains between 12 and 45 percent of the drop in the employment, while declining home equity accounts for an additional 20 percent.

CEO and Governance

Chairman: Alexandre H. (Paris Dauphine University)

ORDERS OF MERIT AND CEO COMPENSATION: EVIDENCE FROM A NATURAL EXPERIMENT

Siming Linus (Bocconi University) - linus.siming@unibocconi.it

Discussant: Zhivotova Evgenia (University of Mannheim)

Governments around the world bestow upon their citizens orders of merit to reward distinguished service. Can orders of merit substitute for the monetary compensation CEOs receive? This question is empirically investigated through a natural experiment: the 1974 legal reform in which Sweden discontinued the conferral of state orders of merit. A difference-in-difference methodology contrasts CEOs of listed firms who had already received an order at the time of the reform (control group) with CEOs of listed firms who had not received an order (treatment group). The main finding is that compensation increases after the reform for the treatment group relative to the control group. Thus, shareholders needed to increase the CEOs' monetary compensation to make up for the loss of a non-monetary incentive provided by the government. This is evidence that orders of merit can act as an important incentive device for CEOs.

THE CORPORATE GOVERNANCE ENDGAME - AN ECONOMIC ANALYSIS OF MINORITY SQUEEZE - OUT REGULATION IN GERMANY

Croci Ettore (Universita' Cattolica del Sacro Cuore) - ettore.croci@unicatt.it ; Ehrhardt Olaf (University of Applied Sciences Stralsund); Nowak Eric (University of Lugano)

Discussant: Siming Linus (Bocconi University)

This paper examines minority squeeze-outs and their regulation in Germany, a country where majority shareholders have extensively used this tool since its introduction in 2002. Using unique data on court rulings and compensations, we analyze a sample of 324 squeeze-outs of publicly listed companies from 2002 to 2011. Large firms with foreign large shareholders are the most likely to be delisted. Positive stock price performance increases the likelihood of a squeeze-out, but operating performance has the opposite effect. Stock prices react positively to squeeze-out announcements, in particular when the squeeze-out does not follow a previous takeover offer. Nearly all squeeze-outs are legally challenged by minority shareholders, either with an action of avoidance or with an appraisal procedure (or both). We find that additional cash compensation is larger in appraisal procedures, but actions of avoidance are completed in less time and offer higher annualized returns. Overall, our evidence suggests that challenging the cash compensation offered in a squeeze-out delivers high returns for minority investors, net of opportunity costs.

PRIDE AND PRESTIGE: WHY SOME FIRMS PAY THEIR CEOs LESS

Maug Ernst (University of Mannheim); Niessen-Ruenzi Alexandra (University of Mannheim); Zhivotova Evgenia (University of Mannheim) - ev.zhivotova@gmail.com

Discussant: Zhao Shan (Grenoble School of Management)

We investigate the impact of measures of firms' prestige on CEO compensation and find that CEOs of more prestigious companies earn less. For example, total CEO compensation is on average 9% lower for firms rated among Fortune's ranking of America's most admired companies. We suggest that CEOs derive social benefits in the form of an enhanced social status if they work for a company that enjoys public admiration, and that boards extract pay concessions for this non-monetary benefit. Results obtain only for firms with independent compensation committees and other measures of strong boards, presumably because weak boards leave rents to powerful CEOs. The effect also obtains for alternative measures of firm prestige and for older CEOs. We perform a range of robustness checks and can exclude several alternative explanations, including that CEOs wish to signal higher status through lower pay, and that our results are driven by career concerns or by owner-CEOs who forego higher compensation.

11h00 Financial Intermediation

Chairman: Refait-Alexandre C. (University of Franche-Comté)

BANK RISK EXPOSURE, BANK FAILURE AND OFF BALANCE SHEET ACTIVITIES: AN EMPIRICAL ANALYSIS FOR U.S. COMMERCIAL BANKS

Ziadeh Noma (University of Limoges) - noma_ziadeh@hotmail.com

Discussant: Jabbour Ravel (Imperial College Business School)

This study investigates the extent to which commercial U.S. banks engage in off balance sheet activities and the possible implication of such engagement on bank risk exposure and bank failure. Given the heterogeneity of banks' off balance sheet activities, I differentiate credit substitute, derivative and credit derivative contracts and study their alternative role on bank riskiness and bank failure. The preliminary results show that different types of off balance sheet activities impact differently bank risk exposure. While credit substitutes are associated with better performance, all derivative contracts including those held for non-trading purposes are associated with an increase in risk exposure.

MORTGAGE SECURITIZATION: THE GOOD, THE BAD, OR THE IRRELEVANT?

Dong Gang Nathan (Columbia University) - gd2243@columbia.edu

Discussant: Ziadeh Noma (University of Limoges)

This research analyzes the effect of mortgage securitization on the real economy and housing market. I estimate the dynamic response of housing risk and real GDP to shocks of mortgage securitization and banks' ownership of mortgage-backed security (MBS), and test three hypotheses suggested in the extant literature. Using structural vector autoregression (SVAR) methodology and cross-sectional analysis, I find that securitization reduces housing risk by completing the market. Interestingly, housing risk increases when commercial banks' ownership of MBS increases. This positive relationship is inconsistent with the agency view of securitization but is consistent with the neglected risk view of mortgage securitization (Gennaioli, Shleifer, and Vishny 2011). The causal inference is drawn from a quasi-experimental design using housing data of bordering CBSA regions in neighboring states with and without the passing of anti-predatory lending laws.

THE IMPACT OF REGULATORY RISK-BASED CAPITAL REQUIREMENTS ON CREDIT CRISES

Cathcart Lara (Imperial College Business School); El-Jahel Lina (Imperial College Business School); Jabbour Ravel (Imperial College Business School) - r.jabbour10@imperial.ac.uk

Discussant: Dong Gang Nathan (Columbia University)

There has been a lot of controversy surrounding the impact of the Basel framework on crises that occurred soon after these standards were spread across the banking industry. Indeed, whereas it is at the heart of the Basel approach, sought by the Bank of International Settlements (BIS) to have a «level playing field» and make banks «safer» entities, the question of whether this goal can be attained through enforcing capital requirements is still contentious. In this research, we look into whether these capital cushions could have single-handedly affected the viability of banks during the 2007-2009 subprime crisis or whether other factors overshadowed the purpose these cushions were set up for in the first place. Our results support the second claim by affirming that the requirements can have contrasting effects on a bank's behavior when combined with some of these other factors which affect its capital position.

11h00 Microstructure

Chairman: Moinas S. (University of Toulouse 1)

PUBLIC NEWS ARRIVAL AND CROSS-ASSET CORRELATION BREAKDOWN:IMPLICATIONS FOR ALGORITHMIC TRADING

Ho Kin-Yip (Australian National University) - kin-yip.ho@anu.edu.au ; Liu Wai-Man (Australian National University);Yu Jing (University of Western Australia)

Discussant: Bart Zhou Yueshen (VU University Amsterdam)

This study models the role of public news arrivals on asset correlation in a trading environment populated by computerized algorithms. The model is empirically tested with the individual stock futures and its underlying spot markets, which are characterized by the mechanical cost-of-carry relation that is typically exploited by algorithmic trading. In normal circumstances, the return correlation between the stock futures and spot quotes is nearly perfect, because futures market makers peg their quotes to those of the underlying by using computerized algorithms. Our simple model predicts that this near-perfect correlation can occasionally break down with two conditions: one, the futures market is less liquid than the corresponding spot market; and two, the uncertainty surrounding the impact of the news on the underlying stocks is sufficiently large. This breakdown occurs because the futures market makers switch from automating the quote-matching process to manually monitor and update their quotes. By employing the comprehensive RavenPack database with firm-level news releases, we test and confirm our model predictions. In particular, the spot-futures return correlation falls as the news uncertainty rises, and this correlation breakdown is more prominent for small-cap stocks. Furthermore, for actively traded stocks, the impact of the news on the breakdown is more intense. If the overall stock market experiences extreme turbulence, however, this impact is weaker. We discuss the implications for the limits of algorithmic trading.

BELIEF-FREE PRICE FORMATION

Horner Johannes (Yale University); Lovo Stefano (HEC Paris) - lovo@hec.fr ; Tomala Tristan (HEC Paris)

Discussant: Ho Kin-Yip (Australian National University)

We analyze security price formation in a dynamic setting in which long-lived dealers repeatedly compete for trading with potentially informed retail traders. For a class of market microstructure models, we characterize equilibria in which dealers' dynamic pricing strategies are optimal no matter the private information that each dealer has about the economy fundamentals. In a generalization of the Glosten and Milgrom model, these equilibria generate price dynamics that are reminiscent of well known stylized facts: price/trading-flow correlation, volatility clustering, price bubble and inventory/inter-dealer trading correlation.

MIDDLEMEN INTERACTION AND ITS EFFECT ON MARKET QUALITY

Menkveld Albert J. (VU University Amsterdam); Bart Zhou Yueshen (VU University Amsterdam) - yueshenbartzhou@gmail.com

Discussant: Lovo Stefano (HEC Paris)

This paper studies a securities market in which high-frequency traders serve as middlemen. Two frictions, inattention and information asymmetry hinder efficient asset reallocation from a low-valuation seller to high-valuation buyers. Middlemen help the uninformed seller find additional buyers (improving welfare). They, however, impair her ability to learn from market activity (reducing welfare). That is, when middlemen trade with one another to find a reselling opportunity, price pressure arises and the seller cannot distinguish it from a fundamental value drop. Overall, only when reselling opportunities are large enough can sufficiently many middlemen improve welfare. The analysis speaks to recent disruptions in electronic markets.

11h00 Portfolio Management

Chairman: Fontaine P. (University of Grenoble 2 - CNRS)

AN ANATOMY OF FUNDAMENTAL INDEXING

De Moor Lieven (Hogeschool-Universiteit Brussel); Liu Fang (Central University of Finance and Economics, Beijing); Sercu Piet M. F. A. (FEB at KU Leuven) - piet.sercu@kuleuven.be ; Vinaimont Tom (City University of Hong Kong)

Discussant: Vestman Roine (Stockholm University and SIFR)

Adherents of Fundamental Indexing (FI) suggest that it is more profitable to base portfolio weights on indirectly size-related indicators like accounting data rather than directly on market caps. In noisy markets `a la Roll (1984), it is argued, underpriced stocks overperform but are underweighted and vice versa, implying a 'drag' which FI claims to avoid. Mixed into the debate is the question whether mispricing is partly identifiable or not, i.e. whether a policy of actively increasing the small-cap weights and vv helps. Carhart style regressions are unable to explain the extra return, but that conclusion is not robust across variant models, and there are substantial doubts about the constantness of factor sensitivities. Cross-sectional regression of weight shifts show that the weight shifts are much larger than necessary to avoid drag and that the cross-sectional patterns are also quite variable over time. In short, not only there are style shifts, but they are also unstable. To estimate the benefits from drag avoidance purged of style shifts without having to rely on generalized FF regressions, our procedure is to sort stocks on size into vigintiles, and compare within each vigintile the performance of FI-weighted returns to equally-weighted (EW) returns, which should be immune to drag too without much style shift. We find that within-vigintile EW portfolios are style neutral w.r.t. market and value, and do not meaningfully outperform VW portfolios. Thus, avoiding drag is not why FI does well: drag is empirically unimportant. Most or all of the prima facie benefits must be from time-varying style shifts.

DO FUND INVESTORS KNOW THAT RISK IS SOMETIMES NOT PRICED?

Irek Fabian (University of Luxembourg); Lehnert Thorsten (University of Luxembourg) - thorsten-lehnert@uni.lu

Discussant: Sercu Piet M. F. A. (FEB at KU Leuven)

Using the sentiment index of Baker and Wurgler (2006), we find that market risk is only a priced factor of expected fund returns when investor sentiment is low. When sentiment is high, the market risk premium becomes insignificant. We then analyze the performance of fund investors in the cross-section of market risk. Although sentiment leads to interesting pattern of funds' returns in excess of the market smart investors seem aware that funds' alphas do not vary with the state of sentiment. One of our key findings is that smart investors prefer the safest funds. The effects we document are economically large: a trading strategy which is long in the positive cashflow portfolio and short in the negative cashflow portfolio yields an annualized alpha of 3.72 percent for the group of safest funds even after controlling for size, book-to-market and momentum.

LIMITED STOCK MARKET PARTICIPATION AMONG RENTERS AND HOME OWNERS

Vestman Roine (Stockholm University and SIFR) - roine.vestman@sifr.org

Discussant: Michala Dimitra (University of Luxembourg)

Home owners are about twice as likely as renters to participate in the stock market, both in the USA and Sweden. This paper sets up a life-cycle portfolio choice model which generates this pattern of limited stock market participation. Calibrated to Swedish data, the model generates the stock market participation rate of home owners as well as the much lower participation rate of renters. In addition, the model replicates two salient features of the data. First, it replicates the U-shaped life-cycle profile of stock market participation among renters, which is due to sorting. Second, the crowding-out mechanism that leads to limited participation among home owners in the model is consistent with difference-in-difference regressions on a high-quality Swedish panel data set.

14h15 Hedge-Mutual Funds

Chairman: Broihanne M.H. (University of Strasbourg)

MONEY FOR NOTHING? UNDERSTANDING VARIATION IN REPORTED HEDGE FUND FEES

Ramadorai Tarun (University of Oxford); Streatfield Michael (University of Oxford) - dphil@michaelstreatfield.com

Discussant: Lambert Marie (HEC Management School, University of Liège)

We analyze the determinants of hedge fund management and incentive fees in a large consolidated hedge fund dataset. We detect time-series variation in fees by concentrating our attention on fund launches, and conditioning fees at launch on fund family characteristics. Larger and better performing fund families launch high fee funds. Funds with high management fees at launch do not perform any differently from low management fee funds, though funds with high incentive fees marginally outperform. Our results are robust to the use of an interval regression technique to uncover the underlying continuous distribution of fees from the discrete reported fees.

MOMENTUM STRATEGIES IN FUTURES MARKETS AND TREND-FOLLOWING FUNDS

Baltas Akindynos-Nikolaos (Imperial College Business School) - n.baltas@imperial.ac.uk ; Kosowski Robert (Imperial College Business School)

Discussant: Streatfield Michael (University of Oxford)

In this paper we study time-series momentum strategies in futures markets and their relationship to commodity trading advisors (CTAs). First, we construct one of the most comprehensive sets of time-series momentum portfolios by extending existing studies in three dimensions: time-series (1974-2002), cross-section (71 contracts) and frequency domain (monthly, weekly, daily). Our time series momentum strategies achieve Sharpe ratios of above 1.20 and provide important diversification benefits due to their counter-cyclical behaviour. We find that monthly, weekly and daily strategies exhibit low cross-correlation, which indicates that they capture distinct return continuation phenomena. Second, we provide evidence that CTAs follow time-series momentum strategies, by showing that time-series momentum strategies have high explanatory power in the time-series of CTA returns. Third, based on this result, we investigate whether there exist capacity constraints in time-series momentum strategies, by running predictive regressions of momentum strategy performance on lagged capital flows into the CTA industry. Consistent with the view that futures markets are relatively liquid, we do not find evidence of capacity constraints and this result is robust to different asset classes. Our results have important implications for hedge fund studies and investors.

HIGHER-MOMENT RISK EXPOSURES IN HEDGE FUNDS

Hubner Georges (HEC Management School, University of Liège); Lambert Marie (University of Liège and Maastricht University) - marie.lambert@ulg.ac.be ; Papageorgiou Nicolas A. (HEC Montreal)

Discussant: Baltas Akindynos-Nikolaos (Imperial College Business School)

The paper singles out the key roles of US equity skewness and kurtosis in the determination of the market premia embedded in Hedge Fund returns. We propose a conditional higher-moment asset pricing model with location, trading and higher-moment factors in order to describe the dynamics of the Equity Hedge (Market Neutral, Short Selling and Long/Short strategies), Event Driven, Relative Value, and Funds of Hedge Funds styles. The volatility, skewness and kurtosis implied in the US options markets are used by Hedge Fund managers as instruments to anticipate market movements. Managers should adjust their market exposure in response to variations in the implied higher moments. We show that higher-moment premia improve a conditional asset pricing model both in terms of explanatory power (R-squares and Schwarz criterion) and specification errors across all Hedge Fund styles.

14h15 Interest Rates

Chairman: Quittard-Pinon F. (EM Lyon Business School)

A MODEL OF THE EURO-AREA YIELD CURVE WITH DISCRETE POLICY RATES

Renne Jean-Paul (Banque de France) - jean-paul.renne@banque-france.fr
Discussant: Rostek Stefan (University of Tuebingen)

This paper presents a no-arbitrage model of the yield curve that explicitly incorporates the central-bank policy rate. After having estimated the model using daily euro-area data, I explore the behaviour of risk premia at the short end of the yield curve. These risk premia are neglected by the widely-used practice that consists in backing out market forecasts of future policy-rate moves from money-market forward rates. The results suggest that this practice is valid in terms of sign of the expected target moves, but that it tends to overestimate their size. As an additional contribution, the model is exploited to simulate forward-guidance measures. A credible commitment of the central bank to keep its policy rate unchanged for a given period of time can result in substantial declines in yields. For instance, a central-bank commitment to keep the policy rate at 1% over the next 2 years would imply a decline in the 5-year rate of about 25 basis points.

ON THE OPTIMAL TYPE AND LEVEL OF GUARANTEES FOR PROSPECT THEORY INVESTORS

Ebert Sebastian (University of Bonn); Koos Birgit (University of Bonn); Schneider Judith C. (University of Muenster) - judith.schneider@wiwi.uni-muenster.de
Discussant: Renne Jean-Paul (Banque de France)

This paper studies prospect theory preferences for life insurance contracts with guarantees. We compare three fairly-priced guarantees, a roll-up, ratchet, and a cliquet guarantee, all of which are extensively employed in real insurance contracts all around the world. The optimal contract is either a pure market investment without guarantee or a roll-up contract with a fixed terminal guarantee. The more sophisticated ratchet and cliquet contracts are never optimal. Moreover, we optimize over the contract parameters and, in particular, study the optimal guarantee level. Depending on preference parameters, this may either be the investor's reference point or a crash insurance that only insures very high losses that occur with small probability. We analyze which elements of prospect theory (reference dependence, loss aversion, or probability weighting) drive our results.

A FRACTAL VERSION OF THE HULL-WHITE INTEREST RATE MODEL

Hainaut Donatien (ESC Rennes School of Business) - das.hainaut@gmail.com
Discussant: Schneider Judith C. (University of Muenster)

This paper develops a new version of the Hull-White's model of interest rates, in which the volatility of the short term rate is driven by a Markov switching multifractal model. The interest rate dynamics is still mean reverting but the constant volatility of the Brownian motion is replaced by a multifractal process so as to capture persistent volatility shocks. In this setting, we infer properties of the short term rate distribution, a semi closed form expression for bond prices and their dynamics under a forward measure. Finally, our work is illustrated by a numerical application in which we assess the exposure of a bonds portfolio to the interest risk.

14h15

International Finance

Chairman: Dumas B. (INSEAD)

FINANCIAL GLOBALIZATION AND RISK SHARING: WELFARE EFFECTS AND THE OPTIMALITY OF OPEN MARKETS

Trzcinka Charles A. (Indiana University); Ukhov Andrey D. (Indiana University) - au53@cornell.edu

Discussant: Van Achter Mark (Erasmus University)

To study the welfare effects of investment barriers and the opening of markets to foreigners, we construct an equilibrium model of international asset pricing without agency costs that allows endogenous market participation among heterogeneous agents. Equilibrium prices and the set of participating and non-participating agents are jointly determined in equilibrium and the ability of agents to choose to participate in the market affects prices of domestic and foreign assets. We examine the welfare effects of non-participation and find that when a country moves from complete segmentation to open markets for foreigners, the cost of capital falls in the domestic market. This is consistent with empirical findings in the international asset pricing literature. Through the endogenous participation mechanism, our model is able to capture sources of economic growth. Contrary to previous models, however, we show that opening markets is not Pareto-optimal and we identify a class of domestic agents whose welfare is lower after the opening of markets. These finding have political economy interpretations and policy implications.

FEEDBACK TRADING AND INTERNATIONAL PORTFOLIO ALLOCATION

Kinnunen Jyri (Lappeenranta University of Technology) - jyri.kinnunen@lut.fi

Discussant: Ukhov Andrey D. (Indiana University)

This paper explores the effect of feedback trading on expected returns and international portfolio allocation using stock market data for the US and Latin America. Autocorrelation in monthly returns are shown to vary with volatility as suggested by the Shiller-Sentana-Wadhwani feedback trading model. While the feedback model fits the data considerably better than a conditional version of the zero-beta CAPM, differences between the feedback model and alternative models with a first-order autoregressive term are more modest. Global factors have no explanatory power for expected returns in addition to the feedback model. Investors can improve their portfolio optimization between developed and emerging stock markets by taking feedback trading into consideration.

FX MARKET ILLIQUIDITY AND FUNDING LIQUIDITY CONSTRAINTS

Banti Chiara (City University London) - chiagioanna@yahoo.it ; Phylaktis Kate (City University London)

Discussant: Kinnunen Jyri (Lappeenranta University of Technology)

Using a broad data set for 20 exchange rates of both developed and emerging markets currencies for 13 years, we find that funding liquidity constraints impact on two different aspects of FX market liquidity, transaction costs and market depth, after controlling for global FX volatility, FX market returns and seasonality. The impact of funding liquidity on FX market liquidity relates to market declines when suppliers to liquidity face capital tightness and during crisis times, when there are severe liquidity dry-ups. There is supporting evidence that the impact of funding liquidity on FX market illiquidity relates also to increases in the demand for liquidity as agents become more risk averse during volatile times.

14h15 Private Equity and Venture Capital

Chairman: Sentis P. (University of Montpellier 1)

GRANDSTANDING VERSUS RENT-SEEKING: THE ROLE OF VENTURE CAPITAL REPUTATION IN IPO MARKETS

Bradley Daniel J. (University of South Florida); Kim Incheol (University of South Florida); Krigman Laurie (Babson College) - lkrigman@babson.edu

Discussant: Moeller Thomas (Texas Christian University)

The first day return for IPOs backed by top VCs firms is double that of non-top VCs IPOs, mostly driven by all-star coverage. All-stars are a scarce resource underwriters allocate to their best clients who bring them repeat business. In exchange, top VCs allow excessive underpricing. Underwriters profit from underpricing vis-à-vis allocation strategies whereas VCs gain from information momentum which allows them to cash-out at higher prices at lockup expiration. Our evidence is consistent with top VCs and underwriters collectively engaging in rent-seeking behavior.

INVESTOR HORIZON AND INNOVATION: EVIDENCE FROM PRIVATE EQUITY FUNDS

Barrot Jean-Noel (HEC Paris) - jean-noel.barrot@hec.edu

Discussant: Krigman Laurie (Babson College)

Investments exploring new ideas typically take more time to payoff than investments exploiting existing ones. Hence, investor with a short term horizon might be tilted towards the latter. I test this idea in the context of private equity funds, which generally have a limited investment horizon contractually fixed ex ante. I use between and within fund variations in investment horizon to do so. I show that funds with a longer horizon select younger companies at an earlier stage of their development, stage investment more and hold on to their investments for a longer period of time. Moreover, companies which receive funding from funds with a longer horizon increase their patent stock significantly more than companies which receive funding from short horizon investors. Altogether, these results provide new evidence on the behavior of private equity funds throughout their life cycle and suggest that investor horizon matters to an important extent for the funding of corporate innovation.

PRIVATE EQUITY FUNDRAISING, FUND PERFORMANCE AND FIRM SPECIALIZATION

Gejadze Maia (Université catholique de Louvain); Giot Pierre (University of Namur); Schwienbacher Armin (Univ. Lille Nord de France - SKEMA) - armin.schwienbacher@skema.edu

Discussant: Barrot Jean-Noel (HEC Paris)

Using a firm-level perspective, this paper studies the effect of specialization on the fundraising activities of private equity firms. In the empirical analysis, we consider two dimensions of specialization: asset class (venture capital versus buy-out) and industry. Using a large sample of US private equity firms, we find that fundraising is accelerated only for follow-up funds within their current area of expertise, but delayed for funds raised outside their area. This suggests that expertise cannot be easily extended to other areas. Further, we analyze the impact of duration between two consecutive fundraising by the same PE firm on the investment speed and the performance of the newly launched fund. We show that for non-specialized firms there exists a trade-off between quick fundraising and the performance of the newly raised fund, which fund investors should mind before committing their capital to the new PE fund.

16h15 Derivatives

Chairman: Le Courtois O. (EM Lyon Business School)

EXPLAINING THE VOLATILITY SURFACE: A CLOSED-FORM SOLUTION TO OPTION PRICING IN A FRACTIONAL JUMP-DIFFUSION MARKET

Rostek Stefan (University of Tuebingen) - stefan.rostek@uni-tuebingen.de

Discussant: Lévy-Véhel Jacques (INRIA)

This paper prices European options in a framework that captures both non-normality of returns and serial correlation within financial time series. The underlying security dynamics are driven by a jump-diffusion process where the diffusion part is fractional Brownian motion while jumps exhibit a double-exponential distribution. These model characteristics suffice to overcome most of the evident drawbacks of the classical Black-Scholes setting, while the parsimony of my model still ensures analytical tractability. Due to market incompleteness, I suggest an equilibrium model à la Brennan (1979). I derive a closed-from solution to the problem, which contains the Black-Scholes pricing formulae and the formulae of Kou (2002) as limit cases. As an intuitive illustration of the model's power, I choose the phenomenon of volatility surfaces: I show that the derived formulae are able to reflect observable patterns of real market data as the model entails a smile over moneyness as well as a non-flat term structure of implied Black & Scholes volatilities.

THE FINE STRUCTURE OF VARIANCE: CONSISTENT PRICING OF VIX DERIVATIVES

Branger Nicole (University of Muenster); Völkert Clemens (University of Muenster) - clemens.voelkert@wiwi.uni-muenster.de

Discussant: Donatien Hainaut (ESC Rennes Business School)

This paper provides a tractable framework for consistently modeling and pricing the two most actively traded options on the Chicago Board Options Exchange (CBOE), namely SPX and VIX options. We derive the dynamics of the CBOE volatility index and give semi-closed form solutions for derivatives on it in a general affine jump-diffusion setup. We compare the implications of several special cases of the general model with the major empirical properties of VIX derivatives and the time-series behavior of the VIX. We show that commonly employed affine jump-diffusion models cannot reproduce the basic patterns observed in the data. The fine structure of the variance process is essential to reconcile the empirical regularities with the theoretical models. We find that both variance jumps and a stochastic volatility of variance seem to be important factors in this respect.

DETECTION OF ARBITRAGE IN A MARKET WITH MULTI-ASSET DERIVATIVES AND KNOWN RISK-NEUTRAL MARGINALS

Tavin Bertrand (Université Paris 1 - Panthéon Sorbonne) - btavin@gmail.com

Discussant: Bernard Carole (Waterloo University)

In this paper we study the existence of arbitrage opportunities in a multi-asset market when risk-neutral marginal distributions of asset prices are known. We first propose an intuitive characterization of the absence of arbitrage opportunities in terms of copula functions. We then address the problem of detecting the presence of arbitrage by formalizing its resolution in two distinct ways that are both suitable for the use of optimization algorithms. The first method is valid in the general multivariate case and is based on Bernstein copulas that are dense in the set of all copula functions. The second one is easier to work with but is only valid in the bivariate case. It relies on recent results about improved Fréchet-Hoeffding bounds in presence of additional information. For both methods, details of implementation steps and empirical applications are provided.

16h15

Financial Econometrics

Chairman: Aït-Sahalia Y. (Princeton University)

CAN INTERNET SEARCH QUERIES HELP TO PREDICT STOCK MARKET VOLATILITY?

Dimpfl Thomas (University of Tuebingen); Jank Stephan (Frankfurt School of Finance & Management) - stephan.jank@uni-tuebingen.de

Discussant : Holcblat Benjamin (Norwegian Business School, BI Oslo)

This paper studies the dynamics of stock market volatility and retail investors' attention to the stock market, where attention to the stock market is measured by internet search queries related to the leading stock market index. We find a strong co-movement of the Dow Jones' realized volatility and the volume of search queries for its name. Furthermore, search queries Granger cause volatility: a heightened number of searches today is followed by an increase in volatility tomorrow. We utilize this finding to improve several models of realized volatility. Including search queries in autoregressive models of realized volatility helps to improve volatility forecasts in-sample and out-of-sample as well as for different forecasting horizons. Search queries are particularly useful in high-volatility phases when a precise prediction is vital.

A STRUCTURAL MODEL OF DYNAMIC MARKET TIMING: THEORY AND ESTIMATION

Detemple Jérôme (Boston University) - detemple@bu.edu; Rindisbacher Marcel (Boston University)

Discussant : Jank Stephan (Frankfurt School of Finance & Management)

This paper derives and analyzes dynamic timing strategies of a fund manager with private information. Endogenous timing strategies generated by various information structures and skills, and associated fund styles are identified. Endogenous fund returns are characterized in the public information of an uninformed observer. Econometric methods for style analysis are developed. New tests of timing skill are proposed and their detection ability is analyzed. An application to a universe of hedge fund indices shows significant timing ability in specific categories of hedge fund styles.

A CLASSICAL MOMENT-BASED APPROACH WITH BAYESIAN PROPERTIES: ECONOMETRIC THEORY AND EMPIRICAL EVIDENCE FROM ASSET PRICING

Holcblat Benjamin (Norwegian Business School, BI Oslo) - benjamin.holcblat@bi.no

Discussant : Detemple Jérôme (Boston University)

Consumption-based asset pricing and other areas have been a challenge to existing inference theories. In this paper, we develop a classical moment-based inference framework with Bayesian properties to tackle this challenge. We prove that there exists an intensity distribution of the solutions to empirical moment conditions over the parameter space. We approximate it thanks to the empirical saddlepoint (ESP) technique. We call the result the ESP intensity. A higher ESP intensity value indicates a higher estimated probability weight of being a solution to the empirical moment conditions. We propose to use the ESP intensity in the same way as posteriors are used in Bayesian inference to obtain point estimators, confidence regions, and define tests. We call this the ESP approach, and explain the rationale behind it. We prove the counterpart of Doob's theorem (i.e., consistency) and Bernstein-von Mises' theorem (i.e., asymptotic normality) for the ESP intensity. The ESP approach provides a unique answer to multiple concerns especially acute in consumption-based asset pricing such as lack of identification and multiple hypothesis testing on the same data set. It also sheds a new light on consumption-based asset pricing, and, in particular, indicates that consumption-based asset pricing theory is more consistent with data than existing inference approaches suggest.

16h15 Financial Markets

Chairman: Viviani J.L. (University of Rennes 1)

THE VALUE PREMIUM IN A LARGE-CROSS SECTION OF TEST PORTFOLIOS

Barras Laurent (McGill University) - laurent.barras@mcgill.ca

Discussant: Cujean Julien (Swiss Finance Institute)

We develop a new asset pricing testing methodology that greatly expands the set of test portfolios. By eliminating the strong factor structure of the 25 Fama-French portfolios used in previous tests, our approach improves the evaluation and comparison of asset pricing models. Armed with this methodology, we examine whether the human capital CAPM and the conditional CAPM capture the «leverage» or «distress» risk associated with high book-to-market firms. The empirical evidence shows that portfolios with high operating and financial leverage tend to have: (i) a positive exposure to human capital risk, and (ii) a market beta that rises in recessions, when the market risk premium is high. Consistent with these findings, these two models are able to partly -- but not fully -- explain the value premium. Overall, this paper helps reconcile the conflicting results obtained in past studies by highlighting the relative merits, as well as the failures of each model.

LEISURE, CONSUMPTION AND LONG RUN RISK: AN EMPIRICAL EVALUATION

Zhang Xiang (Autonomous University of Barcelona) - zhang.xiang@uab.es

Discussant: Barras Laurent (McGill University)

I use a long-run risk model with non-separable consumption and leisure in the preferences to price the cross-section of equity portfolios over 1948-2011 for the U.S. market. I estimate the model factors using a VAR with state variables that predict consumption and leisure growth.I find that growth (big) stocks obtain higher long-run leisure beta but lower long-run consumption beta than do value (small) stocks. Because investors can substitute across time between consumption and leisure, using leisure as a `hedge' and increasing the cost of capital while improving future investment opportunities by decreasing the price of long-run risk, rational long-term investors ask for relatively lower equity premiums for bearing the predominant long-run leisure risk. My model does well, in terms of a variety of criteria, relative to competing models in explaining, for example, spreads between value (small) and growth (big) portfolios.

THE SOCIAL DYNAMICS OF PERFORMANCE

Cujean Julien (Swiss Finance Institute) - julien.cujean@epfl.ch

Discussant: Zhang Xiang (Autonomous University of Barcelona)

A pervasive empirical finding is that mutual fund managers do not maintain their performance. In this paper, I show that social interactions can explain this fact. To do so, I allow a “crowd” of managers to meet at random times and exchange ideas within a rational-expectations equilibrium model. I show that social interactions simultaneously allow prices to become more efficient and better-informed managers to reap larger profits. Yet, social interactions cause managers’ alpha to become insignificant. The main implication is that increased efficiency causes managers to implement passive investment strategies for which they should not be rewarded. In addition, by increasing price informativeness, social interactions produce momentum in stock returns and induce most managers to become momentum traders, consistent with empirical findings.

16h15 Mergers and Acquisitions

Chairman: Aktas N. (Univ. Lille Nord de France - SKEMA)

TARGET FINANCIAL INDEPENDENCE, BARGAINING POWER, AND TAKEOVER PRICING

Jindra Jan (Ohio State University); Moeller Thomas (Texas Christian University) - t.moeller@tcu.edu

Discussant: De Bodt Eric (Univ. Lille Nord de France - SKEMA)

The reliance on external versus internal sources of funds determines firms' degrees of financial independence. Firms that do not depend on external funds for their operations have less trepidation regarding the availability and cost of external financing. Hence, they should be in stronger bargaining positions during takeover negotiations vis à vis acquirers. In a large sample of U.S. takeovers, we examine how target financial independence affects takeover prices. Consistent with the bargaining interpretation of target financial independence, acquisitions of targets with greater financial independence are associated with higher takeover premiums and lower acquirer announcement returns. Target financial independence affects takeover outcomes and is a suitable proxy for target bargaining power. Competition in the market for corporate control of public targets does not eliminate these effects of target financial characteristics.

BID RESISTANCE BY TAKEOVER TARGETS: MANAGERIAL BARGAINING OR BAD FAITH?

Bates Thomas W. (Arizona State University) - thomas.bates@asu.edu; Becher David A. (Drexel University)

Discussant: Schwienbacher Armin (Univ. Lille Nord de France - SKEMA)

We investigate management's motives for rejecting initial takeover bids, and identify the wealth effects of this decision for target shareholders. Contested initial bids are negatively correlated with the relative quality of initial offer premiums and uncorrelated with the presence of target classified boards. The likelihood of higher follow-on offers is decreasing in initial offer quality, but higher when targets have a classified board and when target CEO's have a greater proportion of their personal wealth tied to the close of a transaction. Positive long-run returns to the shareholders of firms that do not ultimately close a transaction suggest that target managers, on average, realize significant performance gains in the absence of a change-in-control event. Our evidence on forced CEO turnover indicates that CEOs who err in failing to close high quality offers realize significant personal costs. Overall, our results provide support for a price improvement motive in contested takeover bids.

WHAT DRIVES THE VARIATION IN TAKEOVER CONTRACTS: THE ECONOMICS OR THE LAWYERS?

Karsten Christel (University of Amsterdam) - c.karsten@uva.nl

Discussant: Bollaert Helen (Univ. Lille Nord de France - SKEMA)

This paper uses proprietary access to 151 takeover contracts to empirically study the provisions that are being used to sell privately held targets. We analyze the factors that drive the variation in two sets of key contract provisions, namely the warranties and covenants granted by the sellers. We find that economic variables account for 39% of the variation in warranties, and for 35% of the variation in covenants. We then show that the styles of law firms ("law firm fixed effects") and those of the involved lawyers ("partner fixed effects") explain a substantial additional part of the variation in the contract provisions. The impact of both law firms and lawyers depends highly on the type of contract provision. Our findings suggest that takeover contracts reflect underlying economic conditions but also the preferences or biases of the involved legal advisors.

ABOUT EUROFIDAI

Eurofidai (European Financial Data Institute) is an academic institute funded by the French National Center for Scientific Research (CNRS). Its mission is to develop European financial databases that are useful to finance academic researchers. That's why Eurofidai works in creating verified, controlled, homogeneous databases over long periods.

Financial databases

- European, Asian and Middle Eastern daily stock data

The current daily stock database covers France (1977-2011), 36 other European countries (1986-2011) and 22 Asian and Middle Eastern countries (1985-2011). This global stocks database consists of more than 220 000 securities. It provides verified and proven data over a long timeframe, which is what sets it apart from other currently available stock databases.

- Indexes & factors

- Traditional indexes for Europe and Asia (1980-2011)
- Indexes calculated by Eurofidai for French (1977-2011), European (1990-2011) and Asian and Middle Eastern countries (1992-2011): 1) General and sector indexes 2) Factors and specific indexes (taking into account market, size & momentum factors)

- Spot and forward exchange rates 1975-2010

- European mutual funds

Eurofidai built a historical European mutual funds database, which has no equivalent in Europe. It contains mutual funds over a long period (1980-2011) and for a large sample of funds (more than 100,000 funds), ensuring a strong diversity of funds in terms of investment strategy and domicile.
This database is divided between funds quoted over the counter and funds listed on organized markets (ETF...) and provides information on prices (net asset value, subscription and redemption prices, dividend...) and information on fund's characteristics (name, type, nature of target investors, currency, issuer, manager, fees, investment policy and fund asset allocation...).

- Corporate actions

Eurofidai provides to its users an organized and classified corporate actions database (1977-2011) for equities and mutual funds, which reports information on corporate events affecting companies (name change, sector change, general meeting, merger, change of capital structure, liquidation, bankruptcy proceedings, class actions…) and their securities (split, issue conditions, purchase/exchange offer…) for more than 150.000 instruments.

High performance computing

To process the data that comprises its databases, Eurofidai has invested in high output computing capabilities. Researchers interested in short term access to high performance and volume computing can call on Eurofidai for its expertise in this domain. Thanks to «cloud computing» technology, Eurofidai can provide researchers with an «on demand» computer cluster for the required duration, without them leaving their office.

Document database

Another Eurofidai mission consists of building a bibliographical database on the research production in European Universities and research centers: finance thesis and working papers since the year 2000, with the link to the original document.

Intraday - BEDOFIH

The BEDOFIH project, which aims to create a European intraday financial database, was selected by an international jury as one of 36 projects within the framework of the «Excellence facilities» (Equipex) program launched by the French government. The BEDOFIH project aims to create a European intraday financial database, which is among the most effective means of precisely assessing how European securities markets work. Research on European financial markets is currently hindered by a lack of available European data. Thanks to the BEDOFIH project, researchers will be able to conduct research based on historical European intraday data, and therefore work toward defining more reliable financial models and new modalities for financial regulation. Regulatory institutions such as the "Autorité des marchés financiers" and the "Direction générale du Trésor, Ministère de l'économie et des finances" support the project.